

103
Y 4. SM: 103-50

THE BURDEN OF ESCALATING WORKERS' COMPENSATION COSTS ON SMALL BUSINESS

The Burden of Escalating Workers' C...

HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS

HOUSE OF REPRESENTATIVES

ONE HUNDRED THIRD CONGRESS

FIRST SESSION

WASHINGTON, DC, SEPTEMBER 29, 1993

Printed for the use of the Committee on Small Business

Serial No. 103-50



SUPERINTENDENT OF DOCUMENTS
NEEDSITARY

JUN 30 1994

BOSTON PUBLIC LIBRARY
SUPERINTENDENT OF DOCUMENTS NEEDSITARY

U.S. GOVERNMENT PRINTING OFFICE

72-935 ➡

WASHINGTON : 1994

For sale by the U.S. Government Printing Office
Superintendent of Documents, Congressional Sales Office, Washington, DC 20402

ISBN 0-16-044172-2

103
**THE BURDEN OF ESCALATING WORKERS'
COMPENSATION COSTS ON SMALL BUSINESS**

4. SM: 103-50

e Burden of Escalating Workers' C...

HEARING
BEFORE THE
COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES

ONE HUNDRED THIRD CONGRESS

FIRST SESSION

WASHINGTON, DC, SEPTEMBER 29, 1993

Printed for the use of the Committee on Small Business

Serial No. 103-50



SUPERINTENDENT OF DOCUMENTS
DEPOSITORY

JUN 30 1994

BOSTON PUBLIC LIBRARY
SUPERINTENDENT OF DOCUMENTS DEPOSITORY

U.S. GOVERNMENT PRINTING OFFICE

72-935 ⇌

WASHINGTON : 1994

For sale by the U.S. Government Printing Office
Superintendent of Documents, Congressional Sales Office, Washington, DC 20402

ISBN 0-16-044172-2

COMMITTEE ON SMALL BUSINESS

JOHN J. LaFALCE, New York, *Chairman*

NEAL SMITH, Iowa
IKE SKELTON, Missouri
ROMANO L. MAZZOLI, Kentucky
RON WYDEN, Oregon
NORMAN SISISKY, Virginia
JOHN CONYERS, Jr., Michigan
JAMES H. BILBRAY, Nevada
KWEISI MFUME, Maryland
FLOYD H. FLAKE, New York
BILL SARPALIUS, Texas
GLENN POSHARD, Illinois
EVA M. CLAYTON, North Carolina
MARTIN T. MEEHAN, Massachusetts
PAT DANNER, Missouri
TED STRICKLAND, Ohio
NYDIA M. VELAZQUEZ, New York
CLEO FIELDS, Louisiana
MARJORIE MARGOLIES-MEZVINSKY,
Pennsylvania
WALTER R. TUCKER III, California
RON KLINK, Pennsylvania
LUCILLE ROYBAL-ALLARD, California
EARL F. HILLIARD, Alabama
H. MARTIN LANCASTER, North Carolina
THOMAS H. ANDREWS, Maine
MAXINE WATERS, California
BENNIE G. THOMPSON, Mississippi

JAN MEYERS, Kansas
LARRY COMBEST, Texas
RICHARD H. BAKER, Louisiana
JOEL HEFLEY, Colorado
RONALD K. MACHTLEY, Rhode Island
JIM RAMSTAD, Minnesota
SAM JOHNSON, Texas
WILLIAM H. ZELIFF, Jr., New Hampshire
MICHAEL A. "MAC" COLLINS, Georgia
SCOTT McINNIS, Colorado
MICHAEL HUFFINGTON, California
JAMES M. TALENT, Missouri
JOE KNOLLENBERG, Michigan
JAY DICKY, Arkansas
JAY KIM, California
DONALD A. MANZULLO, Illinois
PETER G. TORKILDSEN, Massachusetts
ROB PORTMAN, Ohio

JEANNE M. ROSLANOWICK, *Staff Director*
STEPHEN P. LYNCH, *Minority Staff Director*

CONTENTS

Hearing held on September 29, 1993.....	Page 1
---	-----------

WITNESSES

WEDNESDAY, SEPTEMBER 29, 1993

Burton, John F. Jr., director, Institute of Management and Labor Relations Acting Dean, School of Business, Rutgers University, Publisher, John Bur- ton's Workers' Compensation Monitor.....	11
Egge, Jon, member, National Federation of Independent Business, chairman, M.P. Plumbing, Clackamas, Oregon.....	24
Hiatt J., Drew, executive vice president and director of Government Affairs, National Business Owners Association.....	7
Lein, Charles D., President, Landstrom's Original Black Hills Gold Creations, on Behalf of the Board of Directors, National Association of Manufacturers, Accompanied by Mark Stuart, associate director of Risk Management, [NAM].....	16
Reber, Polly, director, Government Relations, Small Business Association of Michigan, on Behalf of the National Small Business United, and Small Business Association of Michigan.....	21

APPENDIX

Opening statements:	
Combest, Hon. Larry.....	45
Flake, Hon. Floyd H.	47
Johnson, Hon. Sam.....	50
Klink, Hon. Ron.....	44
LaFalce, Hon. John J.	39
Meyers, Hon. Jan.....	42
Ramstad, Hon. Jim.....	49
Roybal-Allard, Hon. Lucille.....	52
Prepared statements:	
Burton, John F. Jr.	87
Egge, Jon, with attachments.....	140
Charts	151
Labor Management Discussion on Worker's Compensation	153
Hiatt, J. Drew	53
Lein, Charles D.....	103
Reber, Polly	134

THE BURDEN OF ESCALATING WORKERS' COMPENSATION COSTS ON SMALL BUSINESS

WEDNESDAY, SEPTEMBER 29, 1993

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The committee met, pursuant to notice, at 10 a.m., in room 2359-A, Rayburn House Office Building, Hon. John J. LaFalce (chairman of the committee) presiding.

Chairman LAFALCE. The Small Business Committee will come to order.

Over the next several months, the entire Congress and certainly this committee will be deliberating at great length upon one of the most important issues confronting America: Health care reform.

The impact of President Clinton's health care proposal on small business is certain to be a focal point of the debate and this committee will play a pivotal role in exploring that and related issues. The health care reform package has the potential, not only to enable small businesses to provide health insurance at reasonable cost, but also to reduce related financial burdens that have saddled the small business community for years.

President Clinton is to be commended for taking steps in his health reform proposal to alleviate one such related burden—the burgeoning cost of workers' compensation insurance. It is that specific issue that the committee will explore today.

The purpose of today's hearing is twofold: First, we wish to examine the burden that escalating workers' compensation costs have been placing on small businesses and to come to a better understanding of the nature, the scope, the causes of that problem. Second, the committee wishes to consider the best approach to integrate the health component of workers' compensation into a national health plan.

The high level of workers' compensation premiums, and the rapid rise in those premiums in recent years, have placed an enormous financial burden on businesses, both large and small. In some cases, the costs associated with providing such insurance have become so prohibitive as to force actual closure. Between 1970 and 1992, workers' compensation costs rose from 1.1 to 2.57 percent of the average business's payroll. For small businesses, the percentage can be considerably higher. In 1992, providing workers' compensation benefits cost employers \$62 billion. I am told that figure could easily double by 1995 if current trends continue.

So what is causing this troublesome trend? These costs can probably be attributed to a great number of factors: Higher pay, since most benefits are calculated as a percent of preinjury wages; more generous cash benefits provided by workers' compensation statutes; deteriorating workplace safety; greater fraud in the workers' compensation program; and increased litigation.

But perhaps the most significant contributor to this price escalation has been the skyrocketing cost of health care, which now accounts for approximately 40 percent of workers' compensation costs—up from 33 percent in 1980.

Thus, if we do not address the health care problem, it will be extremely difficult to relieve the severe financial burden that workers' compensation places on small business.

The Clinton administration is making a good faith, serious effort to address this problem. In an attempt to control these costs and ease the financial burden on small business, President Clinton has proposed changes to the workers' compensation program as part of his overall plan to reform the Nation's health care system. The President recommends that we coordinate the workers' compensation health care delivery system with the new health care structure, but not, at this point, to entirely merge those structures.

Under President Clinton's Program, individuals with work-related injuries who are covered by workers' compensation insurance would seek treatment through their alliance health care plan. Workers' compensation insurers, including self-funding employers, would continue to be responsible for the cost of treatment and for reimbursing health plans for services provided. At least that is the way I understand it.

Now, some would advocate a far more radical approach, a complete merger that would entirely remove the medical component from workers' compensation. The President's plan would create a Commission on Health Benefits and Integration to study the feasibility and appropriateness of transferring the financial responsibility for all medical benefits, including those now covered under workers' compensation and automobile insurance, to the new health system.

The rationale for some eventual complete merger is that it might lower what employers pay in workers' compensation premiums by reducing costs associated with medical price discrimination, the filing of claims to cover nonwork-related injuries, lawsuits, and administrative paperwork. Supporters of this approach also argue that merging the two systems would encourage employees to search for low-cost medical care. Currently, there is little incentive for employees to do so because workers' compensation pays 100 percent of medical expenses, unlike group health plans, which require deductibles and copayments.

There are some clear potential benefits to such an approach in terms of cost reduction. Some experts contend that merging the systems could reduce workers' compensation premiums by some 30 percent nationally. But there are also some very real potential problems. Experience at the State level indicates that significant administrative and/or political barriers exist in trying to implement such plans. Moreover, merging an experience-rated workers' compensation system into a community-rated health care system

raises understandable concerns about how to retain the current incentives for employers to provide a safe work environment.

Our Small Business Committee wishes to examine the President's latest recommendation for reforming the workers' compensation program, as well as the concept of fully integrating the medical component of workers' compensation into the new health care structure. I have called together today a distinguished panel of experts to solicit their assistance, their counsel, their advice, and their help on this issue. It is a difficult issue. It is my hope that this hearing will enable our committee and the rest of the Congress and the administration to better assess the impact of workers' compensation and health care reform on small business and, in turn, ensure the creation of work environments that are both more safe and more profitable.

Joining us this morning will be Mr. John Burton, director of the Institute of Management and Labor Relations at Rutgers University. Mr. Burton publishes a monthly newsletter entitled Workers' Compensation Monitor; Mr. Charles Lein, board of directors of the National Association of Manufacturers' and their Small Manufacturers' Forum. He is also president of Landstrom's Original Black Hills Gold Creations in Rapid City, South Dakota; Miss Polly Reber, member of the National Small Business United and also director of Government Relations for the Small Business Association of the State of Michigan; Mr. Jon Egge, a member of the National Federation of Independent Business and chairman of the M.P. Plumbing company of Clackamas, Oregon; and we are especially pleased to welcome to the committee for the first time as a witness Mr. Drew Hiatt, the executive vice president and Director of Government Affairs for the National Business Owners Association, but formerly the staff director for the Minority on the House Small Business Committee.

But before we hear from the panelists, I would like to ask other Members if they have any statement they wish to make.

First, recognize our distinguished Ranking Minority Member, Mrs. Jan Meyers.

[Chairman LaFalce's statement may be found in the appendix.]

Mrs. MEYERS. Thank you, Mr. Chairman. Thank you for holding this hearing on one of the most troublesome and costly programs currently frustrating small business, the workers' compensation system.

Like you, I think workers' comp was built on a noble premise that many workers should be medically treated and financially compensated when they incur injuries on the job through no fault of their own. Similarly, employers should be able to provide this benefit without having to bear frequent, expensive lawsuits, and should be able to help their workers in a way that allows them to predict costs.

The system so far has met the first part of its promise. Information is spotty, but about 91 million workers, or 87 percent, are covered by traditional compensation programs and are, indeed, receiving the benefits and treatment that they deserve.

Unfortunately, the last part of the equation is in shambles. In 1972, it cost an average of \$93 to cover a worker, but by 1987 the

tab had skyrocketed to \$430 per worker. In 1990, the average cost was \$500.

While workers' comp accounted for 1 percent of payroll in 1972, the average percentage of payroll had doubled to 2.1 percent by 1988, with many employers experiencing costs of 3, 4, and 5 percent of payroll. Part of this story lies in this statistic: The average medical claim was \$2,100 in 1981 but leaped to \$5,400 by 1989—a 157 percent increase.

Now, as this suggests, the taproot of the problem lies in escalating medical costs, but ancillary roots extend to increased litigation, primarily over lost wages and the expansion of the types of injuries covered, such as mental stress and carpal tunnel syndrome.

These problems were magnified during the 1980's as State and Federal legislators sought to cap medical costs in other areas such as Medicare, Medicaid, and private health benefits, but left workers' comp alone. As a result, workers' comp became a target for cost shifting because it offered the path of least resistance to medical care. There were few, if any, cost restrictions so providers funneled claims through the workers' compensation system, triggering wide-scale waste, fraud and abuse in several States.

Now, for small businesses, these forces have become manifest in wildly unpredictable and debilitating premium increases. One, two or even 500 percent increases as a percentage of payroll over the last 10 years have not been uncommon. Because the program is mandated, these costs cannot be avoided or curtailed or otherwise managed, leaving the business plans and dreams of small firm owners in shatters. Sadly, these events can be measured in the loss of jobs, opportunities, productivity and compensation.

Mr. Chairman, examining the plight of small business under workers' compensation is most certainly valuable in itself and I commend you for doing so. However, today's hearing may also have a tangential application to health care reform. As we look at workers' comp today, maybe we should think about tomorrow and consider these questions and others about health care: Will the mandates proposed in the Clinton plan lock small businesses into uncontrollable and unpredictable price increases? Second, how will we guard against waste, fraud and abuse? Will replacing private insurance with State-run bureaucracies help our effort or will we merely replace one set of abuses with another?

I might just comment at this point in time, Mr. Chairman, that when we look at the health alliances that are suggested in the Clinton health care plan, if you put all of the money that all of those health alliances control together—and it has oversight by a seven member board in Washington—the money that those groups control is larger than all State budgets combined. It is a trillion dollars, it is a third of the Federal budget, it is a seventh of our entire national economy. Now, that is a tremendous amount of money for them to control and it is going to cause a tremendous growth in bureaucracy.

Third, how do we avoid frivolous claims that add to our costs?

Mr. Chairman, as the old adage goes, those who ignore history are destined to repeat it. The history of workers' compensation boasts noble intentions, some of which have been fulfilled for the good of all of us. But the recent cost of these admirable intentions

have become unbearable not only to small business but to those seeking new jobs and higher wages as well.

Health care, the health care program, too, was born from good intentions, as were many other programs, but in the real world of small business, good intentions just won't pay the bills, they won't meet the payroll costs of new workers, and they won't buy new equipment.

I hope that as Congress considers yet another mandate on the resources of small enterprises, they will keep this in mind. Thank you again, Mr. Chairman, and my thanks to all of the witnesses we are about to hear from.

Chairman LAFALCE. Thank you.

[Mrs. Meyers' statement may be found in the appendix.]

Chairman LAFALCE. Any other Members have any opening statements they wish to make? Mr. Klink.

Mr. KLINK. Thank you, Mr. Chairman.

I am very pleased the Small Business Committee is holding this hearing to discuss the issue of workmen's compensation and how it affects operations of small business. Currently, there are over 90 million employees covered by the various forms of compensation for work-related injury or death and while few argue about the needs for these laws and the protections they offer, the annual cost for providing the security, as the Chairman said in his opening statement, is astronomical.

Within the 4th Congressional District of Pennsylvania, even large companies are finding it very difficult with our State's workmen's compensation laws. Rockwell International recently closed a plant in New Castle, Pennsylvania. We lost 800 jobs with that closing and they cited as the main reason for their leaving compliance with workman's compensation laws being a serious problem. Rockwell claimed only California's workers' compensation laws was more difficult for them to operate under.

Health care costs, of course, as you have heard, now account for 40 percent of the workers' compensation costs. In an effort to curb the costs, President Clinton has offered that health care services covered by workmen's compensation be delivered through an individual's health plan to reduce the duplication and the waste. In Pennsylvania alone, insurance companies now have asked for a 24 percent increase in workmen's compensation costs. While small businesses need relief in these cost escalations, we need to ask ourselves and ask you if President Clinton's proposal is a solution that will work for small business rather than against them.

I look forward to continued discussion on this very important issue in the hopes that we can maintain the assurance that workers' compensation can provide and also ease the financial burden placed on small businesses.

To the witnesses, I apologize. As often happens in this congressional schedule, we have another hearing going on, but it was important for me to come and make an opening statement to you. I look forward to reading the transcripts, and I am very thankful for the Chairman for addressing this issue, one that is extremely important to not only my district but our State and the entire country. Thank you.

[Mr. Klink's statement may be found in the appendix.]

Chairman LAFALCE. Mr. Combest?

Mr. COMBEST. Thank you, Mr. Chairman.

Mr. Chairman, thank you for calling this hearing on the important issue of workers' compensation and the President's health care package. Skyrocketing cost of workers' compensation premiums is another straw destined to break the back of hard-working west Texas business owners.

While the national average for workers' compensation benefits per employee averaged \$387 in 1990, Texas had one of the highest benefits costs at \$645 per employee. Because of the spiraling costs, the State legislature battled for more than three sessions trying to hammer out an acceptable system. Although the current system appears to be a major improvement, it may be declared unconstitutional. I mention this because workers' compensation-like health care reform is an issue which everyone agrees needs fixing, but on which we just cannot seem to agree on the solution.

Most would agree fraudulent claims by unscrupulous employees, doctors and lawyers can account for up to 30 percent of all claims. So I am grateful for the administration that they have taken this small step in at least trying to address this issue.

Discussions have focused on possibly merging the health portion of individual States' compensation programs into a national health program and form a commission to further study other reform options. While only limited details have been released, the complexity of this problem seems to result in many unanswered questions.

What would happen when full mental health benefits are covered under the Clinton health reform? Would all workers be eligible for so-called mental job-stress?

In Texas, I have been told by workers' compensation experts that Federalizing the health component of workers' compensation would wreak havoc on management of the State system. I understand because the health concerns and lost wages portions are so intertwined the efficient management of such a system would almost be impossible.

I oppose efforts to nationalize workers' compensation or splitting sections of the program for Federal Government to regulate. While Wisconsin has a model program, it would be a failure in Texas because of the diversity of workers and vast differences in types of employment.

Last, a commission on workers' compensation was tried in the early 1970's with the results clearly stating that the States should be left to reform this system themselves.

I look forward to today's testimony, Mr. Chairman, and thank you.

Chairman LAFALCE. Thank you.

[Mr. Combest's statement may be found in the appendix.]

Chairman LAFALCE. Any other Members have any statements they wish to make? Mr. Collins.

Mr. COLLINS. Thank you, Mr. Chairman.

I appreciate the opportunity to hear testimony this morning regarding workers' compensation issues. Like some other Members of Congress, I too am a small businessman and I can personally attest to the fact that runaway workers' compensation, coupled with ever increasing Government regulatory burden and taxation, is pushing

many small business people closer and closer to the edge of insolvency.

I am also looking forward to hearing from small business people and representatives about their views on the Clinton health care proposal and how the proposal will affect workers' compensation issues. Thank you, Mr. Chairman.

Chairman LAFALCE. Thank you.

If there are no other opening statements by the Members, I would like to go to the panelists now.

[Messrs. Flake, Ramstad, and Johnson's statement may be found in the appendix.]

Chairman LAFALCE. Ladies and gentlemen, we have five of you and we would like to hear from all of you. We would also like to engage in dialog, a bit of question and answering, so I am going to ask each of you to attempt to confine your opening statement to no more than 10 minutes. If you could do that by reading your statement, fine. If you can do that by summarizing your statement, fine, but under any circumstances, 10 minutes; OK?

My intention was to go from Mr. Burton right down the line. I want to make just one little exception, because we do have the former staff director for the Republican side testifying for his first time. I will call on Mr. Drew Hiatt to open it up and then we will go to Mr. Burton and go right down the line.

Mr. BILBRAY. Mr. Chairman, should we have this witness sworn?

Mr. HIATT. No, those secrets died with me.

Chairman LAFALCE. Mr. Hiatt.

TESTIMONY OF J. DREW HIATT, EXECUTIVE VICE PRESIDENT AND DIRECTOR OF GOVERNMENT AFFAIRS, NATIONAL BUSINESS OWNERS ASSOCIATION

Mr. HIATT. Thank you, very much, Mr. Chairman, and members of the committee, it is a pleasure for me to return to this wonderful committee and to be on the other side to present testimony on this important issue.

We commend you, Mr. Chairman, for your leadership in convening this hearing today to address this growing problem and the horrendous burden of skyrocketing workers' compensation costs on small business. We also appreciate the opportunity to explore this problem with the committee and its scope and severity and also its effect and burden on America's small business owners. We also appreciate the opportunity to comment on the administration's proposal to integrate the medical portion of workers' compensation with its health care plan.

As we look at the workers' compensation system, America's oldest social insurance program, Mr. Chairman, we realize that it is not in a state of crisis, it is in a state of chaos. It has become increasingly clear that the underlying purpose of workers' compensation has been lost. It is no longer an exclusive remedy for work-related injuries and illnesses. It is no longer a no-fault insurance system. It is no longer a system that serves employers and employees.

Fraud and abuse, spiraling medical costs, legal activism and judicial expansion of compensable benefits have conspired to ruin what was once a progressive and balanced system.

Small business owners across this country and in your districts are crying out for relief from the crushing burden of high workers' compensation premiums. These costs, as the Chairman has pointed out, now represent the single fastest growing labor cost and they are strangling small businesses across this country. As a result, many of the small business owners we talked to are no longer striving for success, they are struggling for their survival. They are worried about whether and how long they can survive without relief from this burden.

If labor costs, particularly workers' compensation premiums, continue to rise beyond small business owners' ability to pay them, how much longer will it be before the real consequences of these costs are measured in massive job losses?

Small business is America's leading employer. Today, 6 out of 10 Americans in your district take home a paycheck from a small firm. Small businesses also create all our new jobs. In fact, they are expected to create more than three-quarters of the 43 million new jobs needed over the next 25 years. Unless we do something to relieve the pressure of these high labor costs on small business owners, we will face job losses. This will hurt healthy workers by taking away their jobs and injured workers by taking away medical care and lost wages. We cannot help employees by driving their employers out of business.

As the Chairman has pointed out today, about 96 million Americans, or about 9 out of every 10 workers, are covered by workers' compensation. He has done an excellent job of pointing out, as have other Members today, some of the horrendous costs associated with this.

The Workers' Compensation Research Institute estimates the cost of workers' compensation will reach about \$70 billion this year, and based on the present growth rate trend, this will mean that this cost will triple by the year 2000.

Fraud and abuse, unrestrained medical costs, excessive legal disputes, and judicial expansion of compensable benefits, as I mentioned, all contribute to the soaring costs of workers' compensation costs. I will not dwell on those facts that have been pointed out already, but I do want to illustrate for this committee some of the factors involved in workers' compensation costs and why they go up. I provided two examples here and I would like to read these, if I might. The names of the claimants have been changed to protect their identities, but the facts around each case have not been altered in any way. One is from North Carolina and the other from Louisiana.

Mr. Ed Hughes, who is a cement finisher, was injured while he was pumping concrete. While he was doing that, a steel boom swung around hitting the overhead power lines, resulting in electrical shock to the gentleman and causing a temporary loss of consciousness.

Upon admission to the hospital, Mr. Hughes tested positive for cocaine. Because of this positive test, the insurer thought it would be responsible for the initial medical cost only. But because of at-

torney involvement, it was later determined the positive testing was not a contributing factor in the incident. The insurer did not have a written drug policy in force, therefore, the insurance company was obligated to accept the compensability.

Mr. Hughes continued to complain of pain and headaches and was subsequently evaluated by many different doctors, including an ophthalmologist, orthopedist, neurologist, as well as a neuropsychiatrist. No objective physical findings confirmed his continued complaints.

Surveillance videos showed Mr. Hughes capable of running, jumping, and walking over seven blocks to his residence, all without apparent discomfort. Confronted with the video, the claimant's complaints changed from physical disabilities to psychological problems including decreased appetite, depression, and crying spells. Incredibly, the insurer remains required to pay benefits to this claimant and has spent in excess of \$23,000 to date.

Alan Johns, another example, is a delivery helper who was injured while helping another employee deliver a washer and dryer, and while carrying this appliance down a flight of stairs, he felt pain in his back. He was treated with physical therapy and medication and released to work.

Later, while picking up a refrigerator, he claimed injury to his left shoulder and was treated by the same physician. The diagnosis was cervical and lumbar strain and after much more therapy, medication, and testing, Mr. Johns remained off work. Even though the claimant was video taped throwing objects from a Mardi Gras float in which he stood for more than 8 hours, his physician refused to return him to work claiming it was simply one of Mr. Johns' better days and resulted from the medication he was taking.

Mr. Johns is a high school graduate and a certified bartender, and due to the efforts of his attorney and a treating physician willing to order endless testing, there is no anticipation of his return to gainful employment. To date, this claimant has cost a total of nearly \$23,000 in indemnity, medical, and other related expenses.

So here are some examples of how attorney involvement which we have talked about and how alleged fraud and abuse in these two cases have driven up the cost.

As a first step toward reforming the Nation's workers' compensation system, we would recommend strongly to this committee legislation to establish a national commission to examine the workers' compensation crisis. Such a commission would be comprised of representatives from business, particularly small business; labor; insurance; medicine; law; consumer groups; Federal, State and local government; as well as other concerned groups. The purpose of this panel would be to develop recommendations and to create guidelines for States to follow in enacting broad reforms of workers' compensation laws.

A further goal would be to ensure the system is returned to its historical purpose of serving both employers and employees. We believe this commission would provide a national forum in which to explore the current crisis and offer a platform for reform.

We would not, and I want to underscore this, recommend nor favor legislation to craft a national workers' compensation law.

Such a law, in our view, would be construed as an encroachment upon the traditional rights and responsibilities of States in the adoption and administration of workers' compensation laws.

The National Business Owners Association opposes the administration's proposal to merge the medical portion of workers' compensation with the health care plan. It must be understood by the members of this committee and the Clinton administration that workers' compensation is much more than a medical delivery system; it is an overall workplace disability management system which focuses on achieving maximum medical improvement. Its goal is to ensure injured workers return to their jobs as quickly as possible.

Mr. Chairman, and members of this committee, we have some serious reservations about an integrated approach. First, we believe this approach would lack the incentives to tailor medical programs for insured workers and, second, we are concerned this might also lead to a relaxed attitude toward workplace safety at some companies. Under an integrated approach, employers with good workplace safety records would subsidize employers with poor records and this would be unfair in our view.

Such a plan would encourage cost shifting and higher costs for work-related treatments. Because our health care system generally operates on a fee-for-service basis, we are concerned a fixed-fee system would promote more conservative methods of treatment that would minimize the provider's time and costs. This implies longer periods of disability which, in turn, would mean longer-lasting workers' compensation disability payments and higher costs.

In our view, it is critical from the standpoint of the small business owner that small employers continue to exercise control over medical costs. Studies have shown that when these employers lose control of the medical component, as is likely in any integrated program, wage replacement costs go up.

I believe in examining this problem this committee must also decide how the exclusive remedy provision of workers' compensation will be addressed. If the medical component of workers' compensation is moved into a national health care system, someone would still pay for the benefits, and shifting costs from one system to another does not make them go away.

The National Business Owners Association asked its members in an August 1993 survey on health care reform whether they would favor including the medical portion of workers' compensation in the administration's new health care reform program. The respondents strongly opposed the proposal.

We appreciate the opportunity here today to offer our views on the workers' compensation crisis and the administration's proposal to fold the medical portion of workers' compensation into its health care plan. Mr. Chairman and members of this committee, we look forward to working with you over the coming months to achieve meaningful reform of the Nation's workers' compensation system and to return it to the system it was intended to be: One that benefits employees and employers alike.

I would be pleased to answer any questions you or other members of the committee have at the appropriate time, Mr. Chairman. Thank you.

Chairman LAFALCE. We will withhold our questions until the conclusion of the testimony.

[Mr. Hiatt's statement may be found in the appendix.]

Chairman LAFALCE. Our next witness, Mr. John Burton, acting dean of the School of Business at Rutgers University.

TESTIMONY OF JOHN F. BURTON JR., DIRECTOR, INSTITUTE OF MANAGEMENT AND LABOR RELATIONS AND ACTING DEAN, SCHOOL OF BUSINESS, RUTGERS UNIVERSITY

Mr. BURTON. Chairman LaFalce and members of the committee, I am pleased to testify at your request. You have put before me a formidable task. Most professors and deans are programmed to speak in 50-minute blocks of time. I will do my best, however, to stay within the 10 minutes.

I feel compelled to add to my written testimony, which will only complicate my task. I have a particular interest in this issue because, in connection with the newsletter that I edit, I am a small businessman. I have workers' compensation policies in both New Jersey and New York, and so I can understand some of the financial pressures that small business is under because of workers' compensation costs.

I found the opening statements by the members of the committee quite enlightening. Clearly you have a grasp of the issues that are involved in workers' compensation and that is going to aid me as I very quickly go through my prepared remarks.

The preliminary data for 1992 indicate that nationally the cost of workers' compensation to employers is about \$60 billion and these costs have escalated rapidly in recent decades. They have escalated much more rapidly than payroll. If you go back to 1960, workers' compensation costs were only about 1 percent of payroll. Currently, they are about 2.5 percent of payroll, nationally, as an average for all employers.

There are, of course, variations among the States in these costs. Some States, California, for example, have costs that run three times or more times the cost in some low-cost States, such as Utah or Indiana. Even within particular States there are substantial variations in costs. Manufacturing firms typically have costs that are twice as high as the average cost in a State; and within particular industries there are also very substantial variations in costs due in large part to the reliance on experience rating, which relates an individual employer's premiums to the benefit payments to the employees of that particular firm.

Workers' compensation is a program that already affects most small firms. They are entirely covered in most States. Nationally, about 87 percent of the work force is covered. The studies that I have seen suggest that small business pays an appropriate share of the cost of the program. There is no evidence that small employers, for example, pay more than their fair share of the cost of this particular program. So what is happening to workers' compensation costs in general will obviously affect small business and that is the main focus of the remaining comments I have.

The source of the higher cost of workers' compensation vary through time. In the 1970's, the cost increases were to a large

extent due to rapidly increasing cash benefits. But since the early 1980's, the primary source of higher cost has been escalating medical benefits. For example, between 1984 and 1990, expenditures on medical benefits increased over 15 percent a year while cash benefits went up about 11 percent a year. As noted by others today, that means that the share of all benefits in the workers' comp program accounted for by medical benefits has gone up rapidly and now accounts for about 41 percent of all benefit payments.

Our most recent figures for 1991 indicate that the medical component of workers' compensation accounted for about \$17 billion of benefits.

It is also worth noting it is not just within the workers' compensation program that we see a rapid escalation of medical expenditures. If you compare the growth of medical expenditures within workers' comp with health care expenditures nationally, workers' comp costs over the last 15 years have gone up much more rapidly, particularly in the 5-year period from 1985 to 1990.

So we have a general health care system, which we all know is having cost problems, but workers' comp has an even more intense medical cost problem, which is one of the reasons we are all concerned about reform of that system.

Why is it that workers' compensation is having these higher medical costs? The first level of explanation is that there are higher charges in the workers' compensation system for services than elsewhere in the health care system. There is also evidence that, for similar injuries, workers' compensation patients receive more services than patients in the other components of the health care system. So we have a problem that reflects both higher prices and higher quantity of medical services in workers' compensation.

Why is it that workers' compensation has this unenviable record of high prices and high quantity of services? I indicate in my written testimony that there are several sources. One, source is the providers of health care services. The general health care system has been under increasing pressures in recent decades to limit the quantity and the price of health care.

We can look at HMO's. We can look at limitations on fees being charged in the Medicaid system. All of these cost containment techniques have put a great deal of pressure on health care providers in the rest of the health care system. These cost containment devices have not been used as much within the workers' compensation system in most States, and, as a result, I think there are several consequences.

First, providers who have been squeezed by fee schedules in PPO's or by Medicaid-Medicare fee schedules have an incentive to recoup some of their losses, if you will, by charging more for workers' compensation. Second, the limited use of utilization review in workers' compensation has allowed providers to provide more services in workers' comp than they would for comparable injuries elsewhere; and, third, as cost containment has become more and more of a factor for providers in the rest of the health care system, providers have a strong incentive to have marginal conditions, back disorders notably, classified work-related because they know they will not be subject to as intense scrutiny on the quantity and price

of services that they provide if the workers' compensation program is involved.

Another factor is that workers also influence the choice of where health care is provided, and as workers look outside of workers' compensation, health care has become less attractive in the last decade with the increasing use of deductibles and limits on the duration of health care.

Workers' compensation has retained its essential characteristic as a first dollar system with no limits on medical care, and so from a worker's standpoint it increasingly becomes more attractive to have a marginal condition classified as work-related rather than having it handled through a group health plan.

The third factor that helps explain the high cost of medical care in workers' compensation is that the delivery system for workers' compensation is tied up with litigation over issues of causality and the extent of disability that very often involves medical testimony. So we get doctors involved in workers' compensation on these medical-legal issues.

Finally, there is an argument to be made, and a recent book by Dr. Nortin Hadler at the University of North Carolina has made this argument forcefully, that for certain types of medical conditions, notably back disorders, there is excessive and unwarranted medical treatment throughout the entire health care system. Dr. Hadler also argues that the primary responsibility for the over-treatment in workers' compensation is the insurance carriers who require workers to undertake operations and other forms of treatment that are expensive and indeed are counterproductive to the rehabilitation of workers.

Now, based on this very brief run-through of the problems in workers' compensation, what are some solutions? Some of the solutions have been tried inside the workers' compensation program. There are two traditional ones.

First, the reliance on fee schedules; that is, schedules which limit the amount of dollars that will be paid for various kinds of services. These fee schedules are used now in about half of the States and in many States they have been around for quite a while.

Despite the widespread use of fee schedules, there is only limited evidence on their effectiveness in limiting health care costs in workers' compensation, and the most recent study concluded that the effect of fee schedules on moderating the rate of increase in medical prices is moderate at best.

The second traditional approach to limiting the costs of workers' compensation health care is to limit the employee's choice of physician. The notion is that if you allow the carrier or the employer to control or influence the choice of physician, that you will get lower cost medical care and ultimately lower costs on the entire case.

Again, there are only a few studies of the effectiveness of this approach to cost containment. The recent Pozzebon study that I cite found that the limits on employee's choice of physician were associated with higher medical costs, contrary to the expectations of those who promote such limits. I think that is a very important message that we need to bear in mind as we think about reform.

As I read the evidence, there is almost no support for the notion that giving the insurers or employers control over the choice of

physicians is a way to reduce the cost of health care. Indeed, the evidence runs fairly strong in the opposite direction.

This means that the solutions that have traditionally been tried in workers' compensation to limit health care costs have not worked very successfully. We are now casting around within workers' compensation to try to find more effective ways to deal with this problem. I discuss in my written statement a recent example from Florida, where there is a pilot being used to study the effect of HMO's within the workers' comp system. The evidence suggests that HMO's may be an effective way to control health care costs.

Nonetheless, the magnitude of the problem and the failure of the traditional cost containment devices on health care within workers' comp have led many to think we need to look to broader reforms and not simply focus on changes within the workers' comp system itself. Some of those broader reforms are generically described as 24-hour coverage.

There are a variety of 24-hour coverage plans that have been proposed. The essence is that the work-related test would be removed for cash benefits or for medical benefits or for both. We now have several States—Oregon, Massachusetts, and Florida—that have authorized pilot studies of 24-hour coverage to see whether or not they might, for example, rein in the cost of medical care. Unfortunately, we don't have evidence from those pilots yet but at least there is a great awareness at the States that some broader reforms may be necessary.

Now, the Clinton proposal, in a sense, could be viewed as a variant on 24-hour coverage, although I do not consider it true 24-hour coverage because some distinctions are still maintained between work-related and nonwork-related injuries in terms of the medical care that is provided.

The Clinton administration proposal, as I understand it, is summarized on page 10 of my testimony, and it has already been summarized by others, so I will certainly skip over that in the interest of conserving time. Let me go to a preliminary assessment of the Clinton administration proposal as I have read that this last week.

First, to invoke a cliché that is commonly pronounced by policy analysts, if it ain't broke, don't fix it. I have devoted most of my testimony, however, to demonstrating that the health care component of workers' compensation is broke, and so a fix would be nice.

Second, what would work as a fix is not obvious. I have also spent a good deal of my testimony arguing that the traditional fixes for health care cost problems in workers' compensation, namely fee schedules and limits on the employee's choice of medical provider, appear to be of limited valuable and arguably only aggravate the medical cost problem that they are supposed to help.

Third, one virtue of the Clinton administration plan is the preservation of a financing mechanism for work-related benefits that continues experience rating. I think that is a crucial element and some of the earlier drafts of the Clinton health care reform did not have that feature.

Fourth, the plan prohibits the use of deductibles and coinsurance for the medical care provided for work-related injuries. This prohibition eliminates one of the cost containment devices that has been

shown to be relatively successful in the health care system outside of workers' compensation.

Fifth, the method used to determine the charges for medical care provided by the health plans for work injuries that are reimbursed by the employer concerns me, as does the reimbursement mechanism. The health plans themselves receive fixed premiums based on risk characteristics of their patients so far as nonwork-related injuries are concerned. Coupled with this capitation payment system for nonwork-related injuries is a fee-for-service arrangement for work-related injuries, with the reimbursement of the health plan by the employer based on the amounts established by a fee schedule.

This arrangement seems to invite cost shifting by health plans, which could classify marginal cases as work-related in order to get fee-for-service payments and in order to provide extra services for workers' compensation cases, since it is now not a capitation system but a fee for service system.

Sixth, and perplexing aspect, of the Clinton proposal concerns the ability of employers or carriers to influence the amount and type of health care provided for work-related injuries. The provision of medical benefits is intertwined with the provision of cash benefits, as the previous witness noted, and one danger of any plan that focuses primarily on reducing health care costs is that any savings there may result in a higher cash benefit.

The concern about the loss of control over the health care component of a workers' compensation case, because of the fear of the consequences for the amount of cash benefits, has led to the resistance by some carriers and employers and trade groups to the notion of relying on health plans as the primary source of medical care for work-related injuries. These carriers, or spokesmen, would prefer to keep workers' compensation medical care out of the health plans normally used by workers and in a separate set of health care providers selected by the carriers.

I suspect that these carriers, are making a serious mistake. As I indicated earlier in my testimony, the evidence from the current workers' compensation system suggests that those States that allow carriers to choose the treating physicians have higher medical costs and the strong possibility exists that giving carriers the choice of treating physicians in all jurisdictions would convert a failed policy in selective States into a national failure.

Moreover, there are possible virtues of requiring employees to use the same health plans for work-related injuries as for nonwork-related injuries. Currently, in many States there are networks of doctors who specialize in workers' compensation cases and some of these doctors overtreat and exaggerate the periods of disability and extent of permanent impairment.

The Clinton administration proposal would limit the ability of employees to doctor shop as part of the medical-legal process. I would urge carriers and others who oppose this plan to carefully consider whether they would not be better off surrendering the ability to choose the treating physician, which is of dubious value anyhow, for the advantages of a health plan in which doctor shopping by employees is limited.

Mr. Chairman, I hope this testimony is of value.

Chairman LAFALCE. Well, you have deepened our understanding of the complexities involved.

Mr. BURTON. I take that as a compliment.

Chairman LAFALCE. It is a compliment. It is a compliment.

[Mr. Burton's statement may be found in the appendix.]

Chairman LAFALCE. Our next witness will be a representative from the National Association of Manufacturers, Mr. Charles Lein.

TESTIMONY OF CHARLES D. LEIN, PRESIDENT, LANDSTROM'S ORIGINAL BLACK HILLS GOLD CREATIONS, ON BEHALF OF THE BOARD OF DIRECTORS, NATIONAL ASSOCIATION OF MANUFACTURERS, ACCOMPANIED BY MARK STUART, ASSOCIATE DIRECTOR OF RISK MANAGEMENT [NAM]

Mr. LEIN. Good morning, Mr. Chairman and members of the committee, I am Chuck Lein. With me today is Mark Stuart, associate director of Risk Management for the National Association of Manufacturers.

I am president of Landstrom's Original Black Hills Gold Creations in Rapid City, South Dakota. We are a jewelry manufacturer, and I appear today on behalf of the Board of Directors of the National Association of Manufacturers' Small Manufacturers Forum.

Mr. Chairman, I would like to thank you and the committee today for the opportunity to both discuss the burden of escalating workers comp costs on small business and to discuss the potential benefits and weaknesses of the administration's proposal to integrate the medical component of workers' compensation into a national health care plan. It is an issue that perennially dominates NAM surveys of both small and large manufacturers, and I would note that in our State of South Dakota it is the hottest topic on the agenda for industry and commerce of South Dakota and is one of three top topics for consideration by our State legislature.

Traditionally, the National Association of Manufacturers has long opposed Federal involvement in any way of the State-run workers' compensation system. This remains current NAM policy. We have been, however, willing to discuss ideas that improve the workers' compensation system within the context of a national health care plan.

We are currently evaluating the administration's entire health care proposal and our position on workers' compensation will depend heavily on our position on health care reform. That will be addressed, incidentally, late next week at a board meeting in California.

I would also like to say that the current system, although jeopardized by rapidly rising costs, still serves the majority of claimants well. It is a minority of cases that has driven costs up everywhere.

Before I review the burdens the workers' compensation has on small business, and the pros and cons of the Clinton proposal, I would like to tell you about some of the problems our company faces with the existing system in even a rural State like South Dakota. In essence, what I would like to do, ladies and gentlemen, is bring you back into what it is like in the trenches.

Ours is a relatively small company by many standards, but it is one of the larger jewelry manufacturers in the United States. We have 420 employees in Rapid City, South Dakota, a network of independent reps throughout the United States and several corners of the world. We are not fly-by-nights. We are in the process of celebrating our 75th anniversary.

A decade ago our costs for workers' compensation were relatively insignificant. We have one of the safest, cleanest, most environmentally correct work environments in our industry worldwide. Yet today, we pay more in workers' compensation insurance each month than we paid per year not many years ago.

Chairman LAFALCE. Does that mean that your workers' compensation costs have gone up approximately 1,200 percent.

Mr. LEIN. A part of that, Mr. Chairman, is driven by the fact that our company has grown.

While the vast majority of American workers do not abuse the system, an increasing number has become vulnerable to an abusive, expensive free ride. For example, in California and other States, we have law firm "cappers" hanging around unemployment offices counseling claimants as to how, quote, their possible headaches could be stress related having been brought on by conditions surrounding their employment.

Nationwide, we have consortium of attorneys and physicians advertising on television asking what musicians, grocery store checkers and factory workers share in common. They proceed to describe cumulative trauma, repetitive motion, carpal tunnel injury, and advertise no cost initial consultation.

Physicians are scared to death of malpractice lawsuits. Insurance carriers are not overtly motivated to contain costs, they simply pass through escalating costs to the insured, and an increasing number of attorneys are out trolling for dollars.

Not long ago I became quite concerned when I discovered that we had 11 of 13 active work comp cases in one department on one shift. Almost all were relatively new employees who had all been, quote, stricken with carpal tunnel. My curiosity was further peaked when I learned a new employee was overheard asking what carpal tunnel felt like and how do you get it. Within 30 minutes, he also was stricken. About the same time a lady in her late 20's was declared to be totally disabled by her physician after having been trained as a solderer for only 2 months.

We were so concerned with what was happening that an office employee who had no injury asked if she could test the system. The examining physician's opening question was centered around how much time she wanted off. By the time she was thoroughly examined, she had a medication prescription, braces for both wrists, and was advised she was a whisper away from surgery on both wrists.

I have asked physician friends how this could be. The response has consistently been that if somebody says they hurt, physicians hardly dare challenge that response.

On a personal note, not one representing NAM necessarily, in spite of these and other numerous other horror stories, which most employers have to share, I honestly and personally seriously question the appropriateness or promised efficiency that can accrue from a federally mandated, managed or controlled health care

system. Frankly, without exception, the representation of the Federal Government for cost control and efficiency is nonexistent, while its history of bureaucracy and ever escalating cost is overwhelming.

Also on a personal note, I am reminded how so many small American businesses are on the bubble and their literal survival is at risk. Small businesses fuel the engine of American enterprise. Almost every successful American business today was at one time small and struggling. While he is not a manufacturer, my 27-year-old son is a young retail entrepreneur.

I recently asked Keith how are the numbers working; how did you do last year? He said he was working 80 to 100 hours a week, he paid the mall \$65,000 rent, he made his loan payments, \$45,000 at the bank, and had a work force that seasonally ranged from 5 to 35 employees, and he paid himself—and his wife is working with him, and this is how he can do this—he paid himself \$4,200 for the year, but he is gaining on it.

Ladies and gentlemen, another federally mandated expense will force Keith and many thousands of other small business people to close up shop. American enterprise does not need any more help from the Federal Government.

Mr. COLLINS. Amen.

Mr. LEIN. Now, back to NAM.

There are problems with regard to our ability to retrieve reliable data that differentiates costs for large and small businesses on a historical perspective. Accurate data, as I note, is difficult to obtain.

With few exceptions, all employers are required to purchase workers' compensation insurance to ensure that workers who have become disabled as a result of an on-the-job injury or illness will receive compensation to pay their medical costs and to provide indemnity benefits for lost earnings.

In all but four States, large employers are allowed to self-insure their workers' compensation risks, and about 20 States allow, subject to many stringent requirements, groups of employers to pool their risks under group self-insurance plans.

Most small employers are not allowed to insure through these groups. As a result, most small employers have no choice in most cases but to pay the premium cost quoted by the insurance carrier.

By contrast, many large employers are able to have more than one carrier bidding for their business. While these numbers are not finite, we believe this results in premium costs that are 5 to 10 percent lower than for smaller employers with comparable risks.

In recent years, the escalating cost of workers' compensation insurance for small employers has driven some out of business and caused others to curtail the hiring of additional employees, even though many of them have had no workers' compensation claims filed against them.

For many years the Social Security Administration has published data on the total cost of medical and indemnity benefits nationally and State-by-State. According to their reports, the costs of cash indemnity and medical benefits have almost tripped during the 10-year period between 1982 and 1992.

NAM workers' compensation subcommittee has developed a set of guidelines which it will use to judge the inclusion of workers' compensation in any national health care proposal. My following comments on the pros and cons of integrating the medical portion of workers' compensation reflect an initial analysis by NAM's workers' compensation task force using these guidelines.

I would note that our review generated more questions and comments than it did identifiable pros and cons, so I have listed those comments and questions after our preliminary analysis.

I should also note that States such as Florida, Oregon, and Washington are experimenting with workers' compensation reform programs and we would suggest that it may be premature to implement reform at the Federal level without giving the proper time to determine the effectiveness of these State reform plans.

We did articulate three possible benefits of integrating the medical portion of workers' compensation in a national health care plan. One is fee schedule.

It appears that the administration's proposal may include the application of a fee schedule to workers' compensation injuries. The administration's draft position on this issue indicated this possibility, but it is difficult to determine what the protocols for treatment will be under this plan. Protocols could make or break the effectiveness of the new system.

A second possible benefit centers around negotiated fees, the possibility of negotiated fees with providers for workers' compensation injuries. Under the administration's proposal, it appears that health care providers may be able to negotiate lower fees than the suggested fee schedule.

Third, the proposal does contain a provision that could reduce or eliminate self-referrals. In the current system, self-referrals has aggravated workers' compensation costs.

What are some of the potential problems with the integration of the medical portion of workers' compensation in the national health care plan? There are several.

The ability of the employer to be involved early in the employee's return to work is really a key to the success of any plan.

The administration's proposal appears to reduce employer involvement and control over medical care by mandating that the health alliance play the dominating role as a case manager. This provision could build a barrier between the employer and the employee. A health alliance case manager is not in the best position to advise on the employee's recovery. This task requires an in-depth natural knowledge of the workplace, job requirements and capabilities of the employee. It is best accomplished by employer case managers.

This plan would also affect the ability of the employer to direct specific cases to true specialists for occupational injuries and rehabilitation. All doctors are not equal. Some are better suited to handling these tasks and have experience in workers' compensation. In many cases, employers are familiar with the most effective health providers of work-related injuries and illnesses.

Cost shifting. Under the current workers' compensation system, there are no copays or deductibles, as has been noted previously. The administration's proposal would continue this practice. Many

in the employer community believe the lack of copayments and deductibles for workplace injuries and illnesses and the chance to receive indemnity benefits have long been a source of shifting costs from group health to the workers' compensation system. Again, a point that has been articulated earlier.

The NAM does not endorse and is not suggesting that copays and deductibles be a part of a new system, but we point out that cost shifting is a problem now and would continue to exist under the administration's proposal.

We would also point out under the administration's proposal the provider seems to have no reason to dispute a workers' compensation claim, a perpetuation of a situation described earlier. Treating an injury under the alliance plan would be new revenue to the plan as opposed to treating an injury under regular health insurance which would be a loss to the provider and must be paid out of premiums. Thus, there remains an incentive for the provider to treat an injury as a workers' compensation claim.

Under the administration's proposal, there is a segregation of medical aspects of the State-controlled disability components, which would likely lead to disputes and litigation. Potential difference in plans from State-to-State may create an incentive for employees to switch jurisdictions for claims, which could lead to additional litigation.

A new national system will complicate administration of these claims or of claims for employees working and living in different or multiple States, a very common occurrence in many, many areas of our country. What happens when an employee is injured on a job out of the State in which he or she lives? What if that employee, for example, a severely burned person requires hundreds of thousands of dollars of emergency medical treatment? We are concerned that there will be a dispute between alliances, especially over more costly injuries. The result may well be new litigation between the alliances for such costly treatment.

In conclusion, as we all know, this is an extremely difficult and complex issue to address. I really appreciate the attention that this committee is giving to the issue because it is so critical and it is on the front burner for so many American businesses. We acknowledge that if the health care system is going to be changed, the workers' compensation portion must have been addressed as well. If not, the workers' compensation system will simply be doomed to cost shifting.

NAM will review any health care reform proposal that includes workers' compensation against our guidelines and in the overall context of the health care reform proposal. This review will be provided to the committee when it is available. We will also develop a position on what the manufacturing community would like to see done with the system. It is important to understand that no reform proposal has ever been so seriously considered at the Federal level. We must urge great caution be given to such a discussion and such a decisionmaking process.

The current system, for all its problems, does serve the majority of claimants well. It is a minority of cases, in combination with systemic problems, that have complicated the system. The NAM, along with the AFL-CIO, co-chair the labor management discussion

group on workers' compensation. We have been meeting for more than 2 years on a regular basis.

Our primary focus has been on issues related to the two most important players in the system, the employee and the employer. We have developed white papers which our peers can use at the State level as a guide to solving some of their problems. We will try over the next few months to do the same on this issue.

NAM members are concerned about their employees. People make businesses work. They want to continue to provide them with affordable, high quality health care. Many of the programs voluntarily provided by NAM companies provide the best protection available today in the world at very competitive prices. We hope that the programs developed by the administration will allow us to continue to provide affordable quality care for our employees.

Although some proposals currently under discussion are not necessarily, what the NAM would suggest—we remain willing to explore the concept and trust that our words will carry weight in the legislative process. It should be noted that most of our business and industry associations are opposed to any Federal involvement with State workers' compensation programs.

Mr. Chairman, members of the committee, thank you very much for allowing a country boy from South Dakota to be a part of your day.

Chairman LAFALCE. Well, thank you very much, Mr. Lein, for your excellent testimony.

[Mr. Lein's statement may be found in the appendix.]

Chairman LAFALCE. The bells that you heard about 4 minutes ago indicated that we were being summoned to the Floor for a vote. It happens to be on the continuing resolution for fiscal year 1993. It is a recorded vote and, therefore, I will recess the deliberations of the Small Business Committee and we will reconvene in approximately 15 minutes. At that time, we will hear from Ms. Reber, Mr. Egge, and will have questions from the Small Business Committee.

The Small Business Committee stands in recess for 15 minutes.

[Brief Recess.]

Chairman LAFALCE. The Small Business Committee will come to order.

When the committee recessed, we had just completed hearing testimony of the representative of the National Association of Manufacturers, and we now have Ms. Polly Reber, director of Government Relations for the Small Business Association of Michigan, testifying before us on behalf of the National Small Business United.

Ms. Reber?

TESTIMONY OF POLLY REBER, DIRECTOR OF GOVERNMENT RELATIONS, SMALL BUSINESS ASSOCIATION OF MICHIGAN, ON BEHALF OF NATIONAL SMALL BUSINESS UNITED AND SMALL BUSINESS ASSOCIATION OF MICHIGAN

Ms. REBER. Mr. Chairman, members of the committee, I appreciate the opportunity to appear before you today. My name is Polly Reber, I am director of Government Relations with the Small Business Association of Michigan. Our organization is a private, non-profit, multiservice trade association representing over 6,600 small

businesses across the State of Michigan. While the criterion for membership in our organization is 250 employees or less, the overwhelming majority of our members have 25 or fewer employees, closely reflecting the population of the business community as a whole.

Chairman LAFALCE. Ms. Reber, could you please bring your microphone a bit closer?

Ms. REBER. Yes.

Chairman LAFALCE. Thank you.

Ms. REBER. The Small Business Association of Michigan is also an affiliate member of National Small Business United, in Washington, DC.

The State of Michigan has a relatively good workers' compensation insurance system overall. The problem is we cannot afford it, and the reason is spiraling health care costs. Work comp has long been cited by small businesses as one of the most burdensome costs of doing business in Michigan.

In our first edition of Small Business Barometer, which was in April of this year, a publication which not only measures performance but also tracks the expectations and experiences of Michigan's small businesses, work comp costs was mentioned frequently by small business owners as the aspect of Michigan's business climate which was most negative.

Because it is a function of payroll, it is a disincentive to job creation or expansion. Any decision to hire more employees must be weighed against the negative impact of work comp costs. This is a significant threat to small businesses which are currently the largest producers of jobs, not only in Michigan but also in the Nation.

Small businesses do not enjoy some of the advantages the work comp system extends to larger companies. Besides the obvious advantage of having greater resources to absorb the financial shock of increasing rates, big businesses can form self-insured funds and can negotiate more favorable rates with insurers. While some small employers can and do join group self-insured funds, that option is not available to all small employers.

A small business with a history of few or no worker injuries could end up in a risk pool for their industry and thus pay the increased rate along with companies with higher injury experience. Michigan's small businesses also find themselves at a competitive disadvantage with many other States, most especially Indiana, our neighbor to the south, which has much lower work comp costs.

At a time when small businesses need to grow by expanding into markets in other States, Michigan's work comp make our businesses less competitive due to greater benefit costs.

Over the last decade, Michigan has made significant changes to our work comp system. In the early 1980's, Michigan changed from a State-approved rate classification for businesses to an open rating system whereby every insurance company could file and set their own rates for businesses, introducing competition into the system. Today, Michigan has the second lowest number of businesses, 12.9 percent, in the placement facility for assigned risk, which is the insurer of last resort.

In the late 1980's, Michigan began implementing comprehensive health care services rules and a fee schedule for work comp. The

fee schedule sets a maximum fee a provider may charge for any work comp health care services. The rules established a utilization review process to be the responsibility of the carrier. They include a data collection requirement and a dispute resolution process. It is estimated that the implementation of the rules has saved our work comp system 20 percent per year since their implementation.

Michigan has achieved some degree of success in controlling the dramatic increases within the work comp system. As an example, Michigan is one of only two States, the other being Florida, which has implemented six common cost containment strategies in workers' compensation as identified by the Workers' Compensation Research Institute.

One, limited initial provider choice; two, limited provider change; number three, medical fee schedule; number four, hospital payment regulation; five, utilization review; six, bill review.

Along with rising legal costs, the expansion of job-related injuries in recent years to include such things as stress, carpal tunnel syndrome and age-related ailments has contributed to increased work comp costs. However, the most significant factor has been the spiraling cost of health care in the Nation.

The health care component of work comp accounts for approximately 40 percent of the total costs of work comp. Although Michigan's efforts to address costs have seen results within the larger context of dramatic health care cost increases, our work comp system has become a real financial burden for small business.

As a means to addressing this problem nationally, there have been proposals to integrate the health care component of work comp into a national health care plan. Although this may initially seem like a logical step, there is good reason to be extremely cautious with this idea. First, national health care reform is a monumental task. The complexities and challenges of reform are almost overwhelming. To add the health care component of the workers' compensation system to that task at this time could devastate the system.

Once we begin moving toward reform in health care, there may be a need to bring in the health care components of other systems such as work comp. However, we need to proceed carefully to achieve success in creating an effective, quality health care system first. If reform in health care is achieved, many of the concerns with the health care component of work comp will be addressed. At that point, it will be important to analyze integrating work comp into the system.

Issues such as coordination of benefits and dual coverage are relevant to that discussion. Although work comp health care has increased overall more rapidly than health care in general, it amounts to only about 3 percent of the total health care costs. Second, the goal of the health care component of work comp is a little bit different than the goal of health care in general. When a worker is injured on the job, the work comp system is designed with a goal of getting that worker back to work as quickly as possible.

Work comp must provide indemnity and vocational rehabilitation benefits as well. The health care component is factored into a

system which also includes prevention, disability management, and return to work programs.

Workers' compensation insurance is of great value to small business. It creates responsible means by which employers assist and protect their employees should they be injured on the job. It also contributes to a safer and thereby more productive work environment.

The Small Business Association of Michigan and National Small Business United supports reforms in the work comp system to achieve those ends without financially overburdening a most essential part of our economy—small business—just as it supports reforms in the health care system with similar qualifications. While we desperately need relief in high work comp costs, the method to achieve that may not necessarily be within the parameters of national health care reform.

Thank you.

Chairman LAFALCE. Thank you very much, Ms. Reber.

[Mr. Reber's statement may be found in the appendix.]

Chairman LAFALCE. Our last, but by no means our least, important witness is a representative from the National Federation of Independent Business, Mr. Jon Egge.

Mr. EGGE. Egge.

Chairman LAFALCE. Jon Egge.

TESTIMONY OF JON EGGE, MEMBER, NATIONAL FEDERATION OF INDEPENDENT BUSINESS, CHAIRMAN, M.P. PLUMBING, CLACKAMAS, OR

Mr. EGGE. Mr. Chairman, I am feeling a little like Zsa Zsa Gabor's seventh husband. I know what to do but I am not sure I know how to make it interesting.

Chairman LAFALCE. Well, why don't you try.

Mr. EGGE. I will give it a shot.

Chairman LaFalce, distinguished members of the committee, for the record, my name is Jon Egge. I am a resident of the Portland, Oregon, metropolitan area. I currently manage a small, second generation plumbing company. Our company employees 35 individuals in what I like to refer to as family wage jobs.

I am here today on behalf of over 600,000 fellow NFIB members in this country. NFIB is the largest advocate for small business owners such as myself. NFIB doesn't sell insurance, offer credit cards, do potlucks or golf tournaments. Our mission is to provide you with the best information about issues and how your decisions will impact businesses.

I also serve as Oregon's advisory council chairman. As a small business owner of 25 years and one who pays over \$86,000 in health insurance premiums and over \$48,000 per year in workers' compensation premiums, I believe I speak to you as a qualified witness.

My specific interest in workers' compensation grew out of necessity. In 1985, when our workers' compensation costs skyrocketed, what had been a tolerable expense ballooned to 12.9 percent of our production payroll.

In short, I got religion. Workers' comp religion. I became interested in the legislative process in December of 1989. I was asked by

then-Governor Neil Goldschmidt to participate in a successful revolutionary approach to reform, an approach that has led to a 32 percent overall decrease in cost since 1990, a little less than 4 years.

I will share with you the highlights of that experience and speak to the issue of merging workers' comp and health care. Let me start at the beginning, and I am going to leave some of my figures out because they have been stated before.

A couple that I think are very important: 20 States in this country experienced double digit increases last year. The average for all States was 10 percent. As has been mentioned before, the medical costs amount to about 40 percent—

Chairman LAFALCE. Just out of curiosity, do you have the State of New York? Do you have a table there of all the States?

Mr. EGGE. Yes, I do.

Chairman LAFALCE. Well, if you could—is it attached to your testimony?

Mr. EGGE. No, I am sorry, it is not.

Chairman LAFALCE. If you could give it to the committee staff and we will make a copy of that. I am sure each would like to see our own respective figures.

Mr. EGGE. I have the double digit States, is what I have, a list here.

Chairman LAFALCE. If you will provide that.

Mr. EGGE. We can make the entire list available.

Chairman LAFALCE. Please do so.

Mr. EGGE. Medical costs amount to 40 percent of the system. I think the importance here is that it drives the other 60 percent of the system. Workers' comp medical costs in Oregon account for about 3 percent of the total health care dollars spent in Oregon. Nationally, that is closer to 2 percent.

Even after the reform, Oregon's NFIB members have rated workers' compensation as their number two issue right behind health care. Nationally, our organization, for those employers who have employees, those small businesses who have employees, it rates number two nationally also.

A little about the Oregon story, because I think we have heard enough of the negative today. I will give you a little of the positive of what can be done.

Prior to 1990, Oregon had the eighth highest costs in the country and somewhere in the 40's for benefits. So we, clearly, had a high-cost system that had very little benefit. Some referred to it as the system that was an inch deep and a mile wide. If an injured worker hoped to get the maximum benefit, they had better have a lawyer. Easy to get into but not much for the truly injured workers.

The written comments that we have presented to the committee demonstrate this quite clearly, that Oregon was a poor performer prior to 1990. The Governor gathered seven representatives of labor and seven representatives of management in his basement to reform the system. We started with the question: What would a perfect workers' compensation system look like?

Now, we didn't produce a perfect workers' comp system, because I think everybody at this table will agree that cannot be done. But we made some dramatic changes and the results have been dramat-

ic also: 1991, 12.2 percent decrease in cost; 1992, 11 percent decrease in cost; 1993, 11.4 decrease in cost; and in the 1994 just announced, 4.3 percent decrease in cost, for a 32 percent overall decrease in cost.

While the Nation is headed in this direction, Oregon is headed in the opposite direction.

Now, I think your first question might be, well, that would be easy to do if we would cut down on the available benefits to workers, but that, in fact, is not true. In Oregon, we have been able to increase the benefits to workers. In fact, for those most seriously injured, the scheduled benefits, such as loss of a limb, we have doubled the benefits to workers.

Oregon is very proud of its accomplishment. We now stand 23rd in cost and about 25th in benefits. You can divide the reforms in Oregon into four major areas and I think they all have differing time frames in their benefit to the system.

Chairman LAFALCE. Where are you in your testimony, sir?

Mr. EGGE. This is not—I should have pointed out to you that the written testimony is not what I am presenting.

Chairman LAFALCE. Fine. I wanted to make sure I was not missing something.

Mr. EGGE. The written testimony is very close to what has been said, and we did not want to repeat, but there are a lot more numbers in the written testimony and a lot more background.

Chairman LAFALCE. I didn't mean to inhibit you in any way, I just wanted to follow you.

Mr. EGGE. Good.

It divided it in four areas: Access to the system. There has been a lot of talk about how easy it is to get into the workers' comp system. We limited that access to those workers who were really injured in job injuries. That was an immediate benefit to the system.

Safety, which is maybe arguably the largest benefit is more of an intermediate thing. Takes a little longer for that to get going, but one of the big things we did in safety was to increase our consultive services to businesses. It was the theory that there are a couple of ways you can handle safety, one is with a club, and the other is with some consulting services that business, a lot of businesses really want to cooperate and have a safer work environment.

Our workplace incident rate in the State has gone now, which is evidence that we have prevented the accidents before they happen.

Elimination—elimination I should not say that—but reduction of litigation is an immediate event, but one that we addressed in the reforms. Finally, medical managed care is our long-term solution to workers' comp costs in Oregon.

Now, there has been some discussion, and John mentioned earlier, that there were a couple of ways that have been tried and we have used fee schedules in Oregon for many years and with some not very dramatic results. In fact, immeasurable results.

Choice of physicians, which is a part of our solution, but I think the third alternative is more, in terms of managing the entire case, and that is our approach to managed care in Oregon. Insurance carriers and self-insured employers contract with managed care organizations.

Now, this is not simply designed to drive the fees down. It is not a managed cost organization, it is a managed care organization. There is a very real difference between the two.

Utilization review, cooperative claims management. You can choose the doctor but that does not mean you are going to have any cooperation in terms of managing the claim. In Oregon, we hope that this is going to generate some additional savings. Then, of course obviously, included in these agreements are some cost agreements.

The connection between comp and health care. We talked about 24-hour coverage in the Governor's basement. Now, we met for 5 months talking about reform of the comp system in Oregon. Throughout that 5 months we talked about the medical component and how we might marry that to health care. Our conclusion was that in the 5 months of intensive study we could not come up with the answer and we still don't have the answer.

There are still many questions that the other speakers have alluded to, but an outgrowth out of our reform effort has been the pilot program, which John mentioned earlier, and the pilot program, while I would have guessed would have started with self-insured employers, that has not been the fact. We have actually agreement between our largest carrier, partially, Public Safe Corporation in Oregon, which has about half of the workers' comp cases, and Blue Cross of Oregon. The agreement is a contractual agreement between the carrier and Blue Cross.

This is a coordinated benefit, not an integrated benefit, but the individual worker has the ability to go to one medical provider—Blue Cross lists preferred providers—and be confident they will be covered in either instance, whether it is workers' comp or a health care claim.

The integrated merged approach is much more complex and requires a lot more thought than I think that we are able to give it in this short a notice.

Our members voted in a mandate 63 percent in opposition to marrying workers' comp and health care. Now, I think there are probably as many reasons for that, those answers, as there were answers, but my analysis of that is that is an expression of the fear of our members about what might happen. They know what they are faced with now, in many States they are faced with difficult situations, but to get the Federal bureaucracy involved, as has been previously mentioned, thrusts a great deal of fear into our membership.

Increased Government interference and employer's abilities to manage their cost is something that we see, our members see. Disability and time loss will continue to drive the incentive to make a claim under workers' comp system. The gate needs to be watched. Simply paying for the medical fees on a contractual basis is not enough control over the system to satisfy most businesses.

A choice of provider has been listed as a key component of the administration's health plan, however, medical management is one of the most important elements of any solid workers' comp program, as I have explained before. The employer is experience rated and must have the ability to control their cost.

Managing a workers' compensation claim is different from managing a health care claim. In workers' comp, the issues are prevention, safety, ergonomics, return to work programs. With the health care, it is much more personal issues, life-style, personal habits and the confidentiality of the worker's health record.

I am sure that you are aware that a merged system would create some problems with ERISA. I just bring that up. I am not an expert on ERISA and don't want to pretend to be. There is one absolute, however, and that is our members agree that we do not want a Federal workers' compensation program. That is not a fix for the system.

The quantum leap to full integration. There are no snap-the-finger solutions. My suggestion is to wait for the State pilots to show the way. In Oregon, by January 1994, we expect to have some coordinated plans up and running. I ask you to bear in mind that it is a giant leap of faith to jump from the pilot program of coordinated benefits to a universal integrated workers' compensation health care system.

Chairman LAFALCE. Thank you very, very much.

[Mr. Egge's statement may be found in the appendix.]

Chairman LAFALCE. I think all the panelists have given excellent testimony and one of my primary purposes here is not to have the hearing and solve the problem but to have a hearing and come to a better understanding of the problem and to at least begin to explore some of the options that should be considered not even by this committee but by the administration in finalizing their proposals and perfecting their proposals as we go along. I think that your testimony is going to be very helpful in that endeavor.

Everybody comes to this issue from somewhat different perspectives. For me, there are certain sine qua nons, though. Since I have been in Congress, I have wanted to accomplish the following objectives.

I think we are at the point where we can, in this Congress, pass legislation bringing us a long way toward those goals. I don't think we have ever been this close before. We have never had such major Presidential impetus. What are they? Universal coverage. Not universal access but universal coverage. Every American is covered.

Second, reduce the cost increases. I am not saying roll back the costs, but constrain those future cost increases, hopefully to more than the cost of living adjustments.

Third, simplify the system. It is just too complex. It is too complex for the patient, it is too complex for the business, the employer, it is too complex for any and all health care providers. Of course in doing that, we are going to go a long way to reducing the cost increases in the future, too, because so much of it is the administrative paperwork.

Forth, maintain patient choice of health care provider and fifth, maintain, or even enhance, the quality of health care. I would suspect that most everyone would agree with all of those. Although some might differ on the first one, some might say, well, not universal coverage but universal access. But that is an important distinction, and one that I feel strongly about personally, that it should be universal coverage.

How do we get there? I don't know. The Clinton administration has made certain proposals. What will happen in the Congress? That is uncertain. We have many competing proposals. We have some advocates of a single payer approach. I am a cosponsor of that legislation.

We have advocates of other approaches, too, both Democrats and Republicans, and some of the leading lights on that are Congressman Jim Cooper in the House; Senator John Chafee in the Senate, et cetera. So the proposals that have been advanced will be worked with, cooperated with, attacked from the left and from the right. I personally would not be surprised if because of that fact what we wind up with is going to be pretty close to the proposals, because you have people coming in from both the left and the right on this.

One of the stickiest of issues is going to be the employer mandate and some individuals are calling for an individual mandate, some individuals are saying, there ought to be no mandate. That will have to be worked out.

Let me just ask one question. Is everyone here an employer? You are an employer, Mr. Burton, and you have another hat you wear; Mr. Lein, you are; Ms. Reber, you are not; Mr. Egge, you are. So three of you are.

Do the three of you provide insurance for your employees—Mr. Burton?

Mr. BURTON. Workers' compensation insurance.

Chairman LAFALCE. No, health insurance.

Mr. BURTON. To some I do.

Chairman LAFALCE. To some. So you make it available, then?

Mr. LEIN. Yes.

Chairman LAFALCE. Mr. Lein, you do.

Mr. EGGE. We do.

Chairman LAFALCE. Mr. Egge, you do. OK.

Do you think it is fair that some individuals in competition with you do not? Does that give them a competitive advantage over you; the fact that you are providing insurance when they are not? Mr. Burton?

Mr. BURTON. I think that is an issue. Frankly, the issue that is of more concern to me is availability of health insurance to small employers. Even if you want to provide it, it is very difficult to get it, and so in terms of ranking the order—

Chairman LAFALCE. I am not asking that question.

Mr. BURTON. I understand the issue you are talking about, but I was trying to put the answer in perspective. Yes, I am concerned about that.

Chairman LAFALCE. Mr. Lein, are you concerned about a competitive disadvantage?

Mr. LEIN. There are so many other competitive things to worry about but, no. Our industry has gone from three producers to 18 producers. We had half the market, we have that now, and if this is a part of the total package to attract the best people and hang on to the best people, that is not a worry with regard to the competitive environment.

Chairman LAFALCE. Mr. Egge?

Mr. EGGE. My answer would be no. Our industry dictates that I provide health care, but I will tell you that I provide well above what is—

Chairman LAFALCE. So all your competitors provide health care.

Mr. EGGE. No, not all of them. There are a few who do not. But I consider it to be an advantage to me because I get the best help that way.

Mr. LEIN. Yes.

Chairman LAFALCE. OK, good. Let's suppose—this is a big supposition, but just for the sake of dialog—that the administration plan goes through as thus far proposed, and they have called for coordination of benefits. Not merger but just coordination.

What is the best form of coordination? What should we include in the coordination of workers' compensation benefits in a national health care system and what should we leave out of it? Does anyone want to tell me specifically, do these things and don't do these things? Anybody want to—yes, Mr. Egge.

Mr. EGGE. I would be willing to jump in. I may not have the total answer but I will try to start it off anyhow.

In a coordinated program, I think the essential ingredient is that—we are talking about a contractual agreement between a carrier of workers' compensation and the alliance of health care. That agreement needs to be able to have some requirements by the workers' comp carrier on those health care providers and the alliance. If it is just a fee-for-service event, you have lost total control of the management of the workers' compensation claim.

So, to me, how that is crafted is the key element of any coordinated mandate that happens to come out of this legislation. I am sure there is more.

Chairman LAFALCE. Does anybody else wish to comment on that. Mr. Burton.

Mr. BURTON. Well, one way I would put this, I guess speaking in economist's jargon, is that you need to coordinate the incentives that are existing in the workers' comp system with those in the rest of the health care system. I think one of the problems that potentially the administration's proposal has is that there are vastly different incentives on the providers, depending on whether the injury is work-related or not; that is, if it is a nonwork-related injury, they are going to be paid on a capitation basis, which gives them a strong incentive to be quite parsimonious in providing health care services.

The work-related portion, as I understand the proposal, provides the opposite kinds of incentives because it is a fee-for-service plan. I think that has to be thought about more carefully—whether it is possible to think about a capitation payment scheme of some sort for the work-related injury component. I know this will be complex to do, but I think that is an important thing to do.

I must also just kind of add as a fairly obvious point is that, if this proposal goes through, then I think we have a major dilemma for the workers' comp field, because you are going to, through managed competition, if you will, put tremendous incentives on providers to look for deep pockets. Unless workers' comp is carefully integrated one way or another with the rest of the health care system, we are much more vulnerable than we already are.

I think part of our problem in the recent years has been that workers' comp has been bearing a lot of the cost shifting from the rest of the health care system. So I think this will be a tough call for us as to whether we are better off in or out of the national health care plan. If in, how far in.

Chairman LAFALCE. Well, Mr. Lein, you and/or at least the NAM and NFIB on this panel, have been part of the business community side of the labor-management discussion group on workers' compensation.

Mr. Lein, in your testimony on page 21, you indicated that this group has developed white papers which your peers can use at the State level as a guide to solving some of their problems, and you will try over the next few months to do the same on this issue. By this issue you mean workers' comp. I assume this group you are a participant in is going to work to try to come up with some coordinated approach between labor and management for the best way to coordinate workers' comp and health care reform; is that correct?

Mr. LEIN. That is correct, Mr. Chairman.

Chairman LAFALCE. Do you have a timetable on that? Because you don't have to do integration, you just are to do coordination. Let's suppose we are going to pass this plan, say April or May of next year. That may be optimistic, but have you met yet to discuss this concept of coordination? Do you have a timetable for coming in with your recommendation? How is it going?

Mr. LEIN. Like to ask Mr. Stuart.

Mr. STUART. Sure. We met in the subcommittee with the AFL Thursday of last week and it is extremely complex. We are taking issues that we have not been able to resolve at the State level and now trying to figure out under this information under this proposal at the Federal level how to reduce some of these problems.

It is extremely complex and we are going to meet within a month, but I don't think it will be possible to come up with a solution that we will all be happy, not because we are not trying but because it is so complex. I just, I don't see it happening quickly.

Chairman LAFALCE. Well.

Mr. LEIN. Mr. Chairman.

Chairman LAFALCE. Yes, Mr. Lein.

Mr. LEIN. I think that is the section which is in the back of the materials which were handed out, the subheadings articulate the guidelines with which NAM would judge any proposal.

Chairman LAFALCE. I saw those.

Mr. LEIN. I think those really hit on some incredibly salient points that need to be central in any proposal to come forward as you look at the coordination of benefits.

Chairman LAFALCE. Are those generally accepted by the labor component of this labor-management discussion group?

Mr. LEIN. I believe so. The safety issue, I think on occasion we tend to chew on the wrong end of the stick, perhaps. That is motherhood and apple pie. There is nobody that wants an unsafe work environment.

Chairman LAFALCE. May I suggest that you have your next meeting quickly and that it take place in Norway, and that you come back and we will have a great handshake and we will an-

nounce to the world that you have come up with at least the best way to proceed with a coordinated approach?

We have to do something, and it is best that you people can do it. It will make our job an awful lot easier.

Mrs. MEYERS. Mr. Chairman, I might say that I think as a starting point you might like to look at the Republican health care plan in the House.

Chairman LAFALCE. Sure. I have no problem with that.

Mrs. MEYERS. Which has many of the same components that the Democrat plan has. In other words, it has a basic package of benefits, it has a strong medical malpractice component, stronger I think than the Democrats, but we don't know for sure what that is yet exactly; uniform simplified billing. Those two components alone: People, a lot of providers have said to us that medical malpractice and uniform simplified billing—

Chairman LAFALCE. This group is workers' comp, though.

Mrs. MEYERS. I know, I know—would save billions annually. Finally, an emphasis on wellness. But it has no employer's mandate and it has an employer's mandate to educate and offer to their employees a plan but not to pay for it and then get out of the way. Allow for a great deal more pooling and self-insurance than is going on today.

Now, I think a plan like that is going to be much easier to integrate with existing systems. Maybe not, maybe not, but I would like to have you look at that kind of a plan anyway.

Chairman LAFALCE. Well, may I suggest—I will reclaim my time—that if you have a group on workers' compensation in particular, and if we do have a Presidential proposal for the coordination of workers' comp into this, that the workers' compensation group spend most of its time discussing this issue.

Let me just ask one more question. I was struck in the NFIB's testimony by the great disparity amongst the States. In West Virginia, \$712 was your average workers' comp benefit cost; and in the State of New York, which people think of as a very high cost State, the average workers' compensation benefit cost was \$257. What are some States doing or not doing which give them either relatively high or relatively low workers' compensation costs? Mr. Hiatt.

Mr. HIATT. I will be happy to speak to that, Mr. Chairman.

There are, as many of the witnesses on this panel have pointed out, factors which are beyond the control of the small businesses in managing medical costs. One of the things that we have seen, for example, is the judicial expansion of benefits that contributes to higher costs.

For example, in North Carolina, there have been two decisions that have directly impacted medical costs. One decision basically reversed a previous requirement that after 2 years of paying benefits where there has been no improvement in medical condition an employer does not have to continue paying those benefits. However, a judicial decision came down which now mandates limitless medical care over the lifetime of the employee. That is adding to the cost of medical treatment.

Another decision in North Carolina said workers' compensation would be the only remedy, exclusive remedy, for work-related injuries and illnesses. However, in a recent decision, where there is

cause, for reasons of a reckless workplace reported or safety hazards, employees cannot only demand medical and indemnity benefits, but they can also require compensatory and punitive damages as well. So what you see is that there is an expansion of benefits and there is an expansion of remedies beyond what was intended in the original law.

I think all of these impact directly on medical costs and, of course, if medical benefits are increasing and indemnity benefits are increasing, these will have over time an impact on the cost of workers' compensation premiums. These things are beyond the control of small business owners and their efforts to manage medical costs. So I think these are things that have to be taken into consideration as well.

Chairman LAFALCE. Does anybody else wish to add to that? Mr. Burton?

Mr. BURTON. Mr. Chairman, in your comparison with West Virginia and New York, one major difference is West Virginia has a lot of coal mines and New York does not have too many, and coal mining is inherently a very dangerous industry. I think a better way to compare States is to look at the same set of industries so that you don't confuse the comparisons by industry mix.

I have done this for example, I have done this on Michigan. If you look just at the average premiums in Michigan, it tends to look somewhat more expensive than the national average. That reflects, in part, the fact that Michigan has a concentration of heavy industry, auto and foundries and so on. But if you take a standardized industry mix and compare the same set of industries across States, Michigan turns out to be about the national average in terms of the costs of workers' compensation. So that industry mix is a major factor.

Now, there are certainly other factors influencing costs, and I don't disagree with the fact of statutory differences and interpretation of law make a difference in costs.

Chairman LAFALCE. Well, obviously, Michigan is about in the middle of the automobile industry, but who would be at the top and who would be at the bottom, and are there reasons, and what are the reasons for such great disparities amongst the several States? New York was at relatively near the bottom and everybody thinks New York is such a high State. Are we doing something right in New York?

Mr. BURTON. I would say there are a couple of explanations for New York's record. One is the medical costs in New York appear to be fairly under control. I am not quite sure I know why that is. One possible explanation is that New York is one of the few States that uses the DRG system for hospital reimbursement and uses that for the workers' comp system as well as the rest of the health care system. It is one of only a very few States that use that device in the health care area.

I think the DRG system, if I can generalize, is another form of capitation payment where there is a payment made to the hospital based on the initial diagnosis. I think it shifts the incentives to the hospitals to reduce expenditures on health care. That lesson, is one I have tried to draw out as one of the reasons I have concerns about the proposal that the Clinton administration has put forth

for workers' comp; that is, it is a fee-for-service rather than a capitation payment system.

So one of the reasons why New York is in pretty good shape is directly relevant for what we are talking about today. I think they have some incentives on the health care side that are significant.

The other reason is that New York has had relatively low cash benefits, in recent years. They are well below the national average in terms of statutory level of benefits, despite its reputation as a generous State. In fact, it is one of the laggard States in terms of the statutory level of benefits.

Chairman LAFALCE. Mr. Knollenberg.

Mr. EGGE. If I can add one thing.

Chairman LAFALCE. Sure.

Mr. EGGE. One of the things we did in the Oregon reform was to try to take medical issues out of the litigation process, and some other States have tried this with varying degrees of success, a medical arbiter, so that medical people make the medical decisions.

Prior to 1990, we had a situation where we called them "dueling doctors," and a lot of what was done was in preparation for this duel of doctors in front of a court of law. We have tried to take that out and separate the medical issues, and I think that the by-product of trying to eliminate litigation is we have also cut down a bit on the medical costs.

Chairman LAFALCE. I noticed in Oregon you have \$515, which is just a bit more than double New York's.

Mr. EGGE. Those are 1990 figures.

Chairman LAFALCE. Well, whatever figures you use, yes.

Mr. HIATT. Another factor that might have a bearing on this as well, and the panel here I think would agree with this, and I don't have the figures to show this, but I will tell you it is deterrence. There might be in New York, for example, a greater emphasis placed on safety and loss control programs in individual businesses. One of the most effective things that you need to do to control medical costs is to control the amount of claims that are generated, and the only place you can really do that is in the workplace through the implementation of those kinds of programs.

Chairman LAFALCE. Stronger OSHA enforcement.

Mr. HIATT. Well, I don't think you will hear us clamoring for that today, no.

Chairman LAFALCE. Mr. Burton.

Mr. BURTON. I am sorry to jump in on this issue, but I want to go back to something that was said by Jon earlier about the Oregon experience and the fact that their cost reductions appear, to a large extent, to be due to improved safety in the State. One of the features of that Oregon law that was passed a few years ago is mandatory safety committees involving employees and employers.

I know that is a major controversy in Congress, but we do have some experience from at least one State that suggests that such committees may make a major contribution to reducing workplace injuries and then resulting costs of the workers' comp program.

Chairman LAFALCE. I would imagine that labor would be generally supportive of that. Would management be generally supportive of that, Mr. Burton?

Mr. BURTON. I believe in Oregon they are.

Chairman LAFALCE. How about across the—Mr. Lein, Ms. Reber, Mr. Egge, and Mr. Hiatt?

Mr. LEIN. We have, and I don't want to personify it too much, but we have safety committees everywhere. I was sharing earlier today with Mark—

Chairman LAFALCE. Labor-management?

Mr. LEIN. No, safety committees.

Chairman LAFALCE. Mr. Burton was talking about labor-management safety committees.

Mr. LEIN. Well, they are. They are labor and management combined. Cross sections throughout the organization.

One of the best things that I think we have in the State, and I don't mean to be cynical by any means, but so often when somebody says, hello, I am from the Government, I am here to help you, you just cringe, but through the extension arm of South Dakota State University and their College of Engineering they have a program and you can invite them in to just turn the place upside-down.

We have 1,700 OSHA regulations that we need to comply with, and I look at some of our competitors who don't have 420 employees and it is a major expense for us, but we always say we want to do what is legal and we want to do what is right. But the first test in every decision, in everything that we do, we want to do what is legal. Quite honestly, they have been—and it is a rural State, 700,000 people in the entire State.

But South Dakota State University has this service and they will come out and they will go through the entire plant, and out of the 1,700 regulations last time they were there, they said there are 13 things you need to do. One was put a sign over the door that said this is not an exit. None of the things were material; that would bring us to our feet, but we agreed beforehand. They have a relationship with OSHA and this does work.

The philosophy is if there is something that is just terrible, we agree—and they discover it—it will be reported to OSHA immediately. We have a period of time to respond to whatever they discover to correct those ills and then it is, in turn, shared.

But that is the kind of mood and that is the kind of climate that we need to create. Business is not at war with Government. Government is hopefully not at war with business. We don't want to have an environment that results in injury to workers. We have to be competitive in the world economy, and I think that mandates—there are ways of achieving goals. It is kind of like the way you lead a group of employees. You can command them to do something, but if you help them to do the right things and the mood is right, everybody wins.

Mandates, folks, go down hard. There are areas where we need to mandate some things, but the further we move in that direction, in driving mandates for everything into the workplace, into the schools, into whatever it may be in our personal lives, I think we move in the wrong direction.

Mr. EGGE. To answer the question specifically, I was there for the negotiation when we talked about mandatory safety committees in Oregon in the Governor's basement, and businesses' posi-

tion was more from the angle of let us make it so it works, kind of what Mr. Lein has indicated.

It is going to be a mandate. We didn't have a particular problem with that. We thought it was a good idea. It was labor's issue. But we wanted to make sure it worked. I think it works reasonably well. But our membership generally, it can be said that we don't like mandates. So I don't want to speak on behalf of our entire membership, but I will tell you that most employers in Oregon will now tell you, it was worth it.

Chairman LAFALCE. We are going to have to go on. Mr. Knollenberg.

Mr. KNOLLENBERG. Thank you. This business of shifting cost, and I am looking at this sheet that was just passed out. That is sort of interesting to me, the increases, and I presume there is another sheet with decreases but maybe there are not too many people.

Chairman LAFALCE. They are on top.

Mr. EGGE. On top.

Mr. KNOLLENBERG. Oh, I am sorry, they are on top.

I have a question. Maybe you know the answer and maybe you don't. I know, Ms. Reber, you spoke to the fact in Michigan, somewhere in my notes here, you mentioned that the rules you have established have saved 20 percent. The rates here have gone up 11 percent.

Now, with this shifting of cost from group health to workmen's comp. I have to believe there is a great movement in that direction, and because of the fact that with group health you do have copays and they are growing. They are not in place everywhere, but certainly with the Big Three it is a challenge right now to get the folks in organized labor to accept any kind of copay or deductible.

I assume some of that shifting of cost has come from health into workmen's comp. I guess to the extent that that has happened, and maybe you don't have any data on that, and, frankly, there is another question I could ask regarding the Clinton administration and what you see in their reform program that would even speak to the idea of copays and deductibilities on workmen's comp. I know that is a strange concept when you look at the status of the employer and the employees. If the employee gets hurt on the job, he expects to be compensated entirely.

But coming back to the shifting of cost, is there any statistical indication, let's say in Michigan, for example, or Oregon, or from any one of you, as to the shift being real? And would we, if we were to get figures on the cost of health care in the various States, would that have any kind of correlation at all if it were isolated? Do you follow? Are you with me on the question?

In other words, has the shift been great, and if so, how great? Does the deductible copay concept, would that work in the workmen's comp arena?

Mr. EGGE. I can tell you that there is no evidence that is in a scientific form, in a study or anything like that, unless John knows something I don't know, that would tell what these numbers are, that the incentive is to go into workers' compensation and make a claim. But I would tell you if I had no coverage outside of workers' compensation, I would be looking at, seriously, at getting coverage

for an injury or illness. The incentive is obvious and I think there is obvious abuse of that across the United States.

The issue of copays and deductibles in workers' compensation, I don't want to speak on behalf of organized labor, but I will tell you in Oregon that was a walk-out-of-the-room issue. We will not discuss that kind of thing. It was so much so that way that their response was, we will be willing to talk about it under one circumstance only, and that is if you remove the exclusive remedy. Well, that was a walk-out-of-the-room issue for the other side.

So that was an Oregon standoff and we didn't breach that issue beyond that. About that long a discussion. I don't see it as being a serious event in this outcome of this proposal.

Chairman LAFALCE. I suspect you are right.

Mr. KNOLLENBERG. I think you are right, too. The only thing that I would look at, too, though, as somebody mentioned, Mr. Egge, I believe, mentioned this in his testimony, that the big area of concern is a definition of compensable injuries and illnesses.

I have to believe States are all over the block on this one. There is no consistency about that and there has been, as was testified by I think each of you, growth in those new kinds of what is it and how can I get it? I don't know who made that comment but I think that was pretty much the point. There are people who are interested in let me know how I do it and I will do it. So I think there is some concern about a definition.

If I can take another minute, Mr. Chairman, and I don't want to talk about a national program of this kind, but that is what we are talking about, obviously folding it into a national program, but what kind of definition? Are they misusing? Are they misinterpreting? They are obviously taking advantage of whatever definition is there, because that kind of, that exotic injury is on the rise and how do we challenge that?

Mr. LEIN. I did not tell one slice of one story. The lady who was declared to be disabled after 2 months on the job of training to be a solderer. Her husband was also totally disabled and working for, had been working for a packing plant. They are both in their late 20's. He was on total disability but he is still able to hunt, fish, play golf, play slow pitch softball, and garden.

I guess——

Mr. KNOLLENBERG. In that order.

Mr. LEIN. I am not sure what the order was, but I think—and I don't know what the magnitude is of those who are beating the system. The vast majority of American workers have the same philosophy that I described. They don't want to screw the world. They are saying, I am here to do a job, et cetera. But if we make it easy to abuse the system, and if in fact they look around, those temptations are there.

Now, I guess this is one of the fundamental concerns that I have about this whole issue, and it is one of the things that motivated me to respond to the opportunity to come here, is that who is responsible for cost containment? Who is responsible for that?

We have gone to a self-insurance format in our company. We went out to bid. We had a whole raft of companies that sought to, commercial carriers, who sought to bid on our plan again this year. We had gone out to bid 2 years earlier, had the same experience.

The self-insurance format is saving our employees a lot of money, but we have driven the responsibility into the organization. There are incentives for them. If they discover errors in billing, there are financial rewards to them to detect those errors.

We make a big deal of it. If somebody, and it is not malicious on the part of the hospital or whatever it may be, but if somebody gets a \$500 cash reward, that is a positive incentive for—they are controlling themselves.

We had gone from a format where it was too darned easy. Any time anybody had a cold, they could, for \$5 bucks, go see the doc. This is one of the concerns I have as we move in this direction. If it is a free lunch and nobody is responsible, I think that we really have something that will run away from us.

I will tell one other story——

Chairman LAFALCE. Well, I am afraid I will have to limit you on stories.

Mr. LEIN. OK, New Zealand another day.

Mr. KNOLLENBERG. I do appreciate the opportunity to have an extra minute or so, Mr. Chairman. I appreciate the testimony of the entire panel, so thank you very kindly.

Chairman LAFALCE. Some time constraints. I am late, very late, by 25 minutes, for a meeting. But I want to thank the panelists. Your testimony has been very, very helpful.

This is an extremely complex issue, and I appreciate this, but we are making an effort to deal with it. Mr. Burton has said the system is broke and it needs fixing. I was talking about the workers' compensation system now, and we have some efforts that are being made by the President of the United States to help fix the system. To help. Not to fix it, but to help fix it, make it better, prevent it from getting worse. Some embryonic steps—coordination that can be followed after studies and commissions I look forward to working with you in the future to develop a solution.

But not the distant future. We are talking about the next months, now. This is not something that we can delay. I would hope that the next meeting of your labor management group would not be a month from now. That is a month wasted. I would encourage you to meet every 2 weeks or so, set more rigid timetables.

We want to act. There is a tremendous desire on the part of a great many individuals in Congress who have been here a number of years. I am talking about Danny Rostenkowski, the John Dingells, the Ted Kennedys, the George Mitchells, and individuals such as myself, to seize this opportunity.

We will pass a bill. We will pass a bill. We are not going to let this opportunity fall through our hands. So we want to work with you to make it the best bill we can.

Thank you very much.

[Whereupon, at 12:40 p.m., the committee was adjourned, subject to the call of the Chair.]

APPENDIX

OPENING STATEMENT OF THE HONORABLE JOHN J. LaFALCE
CHAIRMAN, COMMITTEE ON SMALL BUSINESSHearing on Workers' Compensation
September 29, 1993

Over the next several months, the Congress and this Committee will be deliberating at length upon one of the most important issues confronting the United States: health care reform.

The impact of President Clinton's health care proposal on small business is certain to be a focal point of the debate, and this Committee will play a pivotal role in exploring that and related issues. The health care reform package has the potential, not only to enable small businesses to provide health insurance at reasonable cost, but also to reduce related financial burdens that have saddled the small business community for years. President Clinton is to be commended for taking steps in his health reform proposal to alleviate one such related burden -- the burgeoning cost of workers' compensation insurance. It is that specific issue that the Committee will explore today.

The purpose of today's hearing on workers' compensation is two-fold: first, to examine the burden that escalating workers' compensation costs place on small business; and second, to consider the best approach to integrate the health component of workers' compensation into a national health plan.

The high level of workers' compensation premiums -- and the rapid rise in those premiums in recent years -- have placed an enormous financial burden on businesses, both large and small. In some cases, the costs associated with providing such insurance have become so prohibitive as to force actual closure. Between 1970 and 1992, workers' compensation costs rose from 1.1 percent to 2.57 percent of the average business's payroll. For small businesses, the percentage can be considerably higher. In 1992, providing workers' compensation benefits cost employers \$62 billion. That figure could easily double by 1995 if current trends continue.

What is causing this troublesome trend? These soaring costs can be attributed to a number of factors: higher pay -- since most benefits are calculated as a percent of pre-injury wages; more generous cash benefits provided by workers' compensation

statutes; deteriorating workplace safety; greater fraud in the workers' compensation program; and increased litigation. But the most significant contributor to this price escalation has been the skyrocketing cost of health care, which now accounts for approximately 40 percent of workers' compensation costs -- up from 33 percent in 1980.

Thus, if we do not address the health care problem, it will be extremely difficult to relieve the severe financial burden that workers' compensation places on small business.

The Clinton Administration is making a serious effort to address this problem. In an attempt to control these costs and ease the financial burden on small business, President Clinton has proposed changes to the workers' compensation program as part of his overall plan to reform the nation's health care system. The President intends to "coordinate" the workers' compensation health care delivery system with the new health care structure -- but not to entirely merge those structures.

Under President Clinton's program, individuals with work-related injuries who are covered by workers' compensation insurance would seek treatment through their alliance health care plan. Workers' compensation insurers (including self-funding employers) would continue to be responsible for the cost of treatment and for reimbursing health plans for services provided. Some would advocate a more radical approach -- a complete merger that would entirely remove the medical component from workers' compensation. The President's plan would create a Commission on Health Benefits and Integration to study the feasibility and appropriateness of transferring the financial responsibility for all medical benefits (including those now covered under workers' compensation and automobile insurance) to the new health system.

The rationale for a complete merger is that it would lower what employers pay in workers' compensation premiums by reducing costs associated with: medical price discrimination, the filing of claims to cover non-work-related injuries, law suits and administrative paperwork. Supporters of this approach also argue that merging the two systems would encourage employees to search for low-cost medical care. Currently, there is little incentive for employees to do so because workers' compensation pays 100 percent of medical expenses -- unlike group health plans, which require deductibles and co-payments.

There are some clear potential benefits to such an approach in terms of cost reduction. Some experts contend that merging the systems could reduce workers' compensation premiums by some 30 percent nationally.

But there are also some real potential problems. Experience at the state level indicates that significant administrative and/or political barriers exist in trying to implement such plans. Moreover, merging an experience-rated workers' compensation system into a community-rated health care system raises understandable concerns about how to retain the current incentives for employers to provide a safe work environment.

The Committee wishes to examine the President's latest recommendation for reforming the workers' compensation program, as well as the concept of fully integrating the medical component of workers' compensation into the new health care structure. I have called together today a distinguished panel of experts to solicit their assistance and advice on this issue. It is my hope that this hearing will enable the Committee to assess the impact of workers' compensation and health care reform on small business, and in turn, ensure the creation of work environments that are safe and profitable. Joining us here this morning are:

* Mr. John Burton, Director, Institute of Management and Labor Relations at Rutgers University. Mr. Burton publishes a monthly newsletter entitled, John Burton's Workers' Compensation Monitor.

* Mr. Charles Lein, Board of Directors of the National Association of Manufacturers' Small Manufacturers Forum and President/CEO of Landstrom's Original Black Hills Gold Creations in Rapid City, South Dakota.

* Ms. Polly Reber, Member, National Small Business United and Director of Government Relations, Small Business Association of Michigan.

* Mr. Jon Egge, Member, National Federation of Independent Business and Chairman, M.P. Plumbing, Clackamas, Oregon.

* Mr. Drew Hiatt, Executive Vice President and Director of Government Affairs, National Business Owners Association.

Opening Statement
U.S. Rep. Jan Meyers (R-KS)
House Committee on Small Business
Workers' Compensation
September 28, 1993

Mr. Chairman, thank you for holding this hearing on one of the most troublesome and costly programs currently frustrating small business, the workers' compensation system.

Like you, I think workers' comp was built on a noble premise: That workers' should be medically treated and financially compensated when they incur injuries on the job through no fault of their own. Similarly, employers should be able to provide this benefit without having to bear frequent, expensive law suits, and should be able to help their workers in a way that allows them to predict costs.

The system, so far, has met the first part of its promise. Information is spotty, but about 91 million workers, or 87 percent, are covered by traditional compensation programs and are indeed receiving the benefits and treatment they deserve.

Unfortunately, the last part of the equation is in shambles. In 1972, it cost an average of 93 dollars to cover a worker, but by 1987, the tab had skyrocketed to 430 dollars per worker. In 1990 the average cost was 500 dollars. While workers' comp accounted for 1 percent of payroll in 1972, the average percentage of payroll had doubled to 2.1 by 1988, with many employers experiencing costs of 3, 4 and 5 percent of payroll.

Part of the story lies in this statistic: The average medical claim was \$2,100 in 1981, but leaped to \$5,400 by 1989 -- a 157 percent increase.

As this suggests, the tap root of the problem lies in escalating medical costs, but ancillary roots extend to increased litigation (primarily over lost wages) and the expansion of the types of injuries covered, such as mental stress and carpal tunnel syndrome.

These problems were magnified during the 1980's as state and federal legislators sought to cap medical costs in other areas, such as Medicare, Medicaid, and private health benefits, but left workers' comp alone. As a result, workers' comp became a target for cost shifting because it offered the path of least resistance to medical care. There were few, if any, cost restrictions, so providers funneled claims through the workers' compensation system, triggering wide-scale waste, fraud, and abuse in several states.

Mrs. Meyers
Page 2

For small businesses, these forces have become manifest in wildly unpredictable and debilitating premium increases. One, two or even five hundred percent increases in premiums as a percentage of payroll over the last ten years have not been uncommon. And because the program is mandated, these costs cannot be avoided, curtailed, or otherwise managed, leaving the business plans and dreams of small firm owners in shatters. Sadly, these events can be measured in the loss of jobs, opportunities, productivity, and competition.

Mr. Chairman, examining the plight of small business under workers' compensation is most certainly valuable in itself, and I commend you for doing so. However, today's hearing may also have a tangential application to health care reform. As we look at workers' comp today, maybe we should think about tomorrow and consider these questions, and others, about health care:

o Will the mandates proposed in the Clinton plan lock small businesses into uncontrollable and unpredictable price increases?

o How will we guard against waste, fraud and abuse? Will replacing private insurance with state-run bureaucracies help our efforts, or will we merely replace one set of abuses with another?

o How do we avoid frivolous claims that add to our costs?

Mr. Chairman, as the old adage goes: "Those who ignore history are destined to repeat it." The history of workers' compensation boasts noble intentions, some of which have been fulfilled for the good of us all. But the recent costs of these admirable intentions have become unbearable, not only to small business, but to those seeking new jobs and higher wages as well.

Health care, too, was born from good intentions, as were many other programs. But in the real world of small business, good intentions won't pay the bills. They won't meet the payroll costs of new workers and they won't buy new equipment. I hope that as Congress considers yet another mandate on the resources of small enterprises, they will keep this in mind.

Thank you, again, Mr. Chairman, and my thanks to all of the witnesses we are about to hear from.

OPENING STATEMENT OF
REP. RON KLINK
COMMITTEE ON SMALL BUSINESS
HEARING ON WORKERS' COMPENSATION

SEPTEMBER 29, 1993

Thank you Mr. Chairman. I am pleased that the Small Business Committee is holding this hearing to discuss the issue of workers' compensation and how it affects the operations of small businesses.

Currently, there are over 90 million employees covered by the various forms of compensation for work-related injury or death. While few argue about the need for these laws and the protection they offer, the annual costs for providing this security is over \$40 billion. Approximately \$30 billion a year are provided as compensation benefits.

Within the 4th Congressional District of Pennsylvania, even large companies find difficulty with the state's worker compensation laws. Rockwell International recently closed a plant in New Castle, Pennsylvania citing compliance with workers' compensation law as a serious problem. Rockwell claimed only California's worker compensation law was more difficult to operate under.

Health care costs now account for 40 percent of workers' compensation costs. In an effort to curb costs, President Clinton has offered that health care services covered by workers' compensation be delivered through an individual's health plan to reduce duplication and waste.

In Pennsylvania alone, insurance companies have asked for a 24 percent increase in workers' compensation costs. While small businesses need relief in these cost escalations, we should ask ourselves if President Clinton's proposal is a solution that will work for small businesses rather than against them.

I look forward to discussing this very important issue in the hope that we can maintain the assurances that workers' compensation provides and also ease the financial burden placed on small businesses.

LARRY COMBEST
19TH DISTRICT TEXAS

COMMITTEE ON AGRICULTURE
COMMITTEE ON SMALL BUSINESS
PERMANENT SELECT COMMITTEE
ON INTELLIGENCE

ROOM 1511
LONGWORTH HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-4319
(202) 225-4005

Congress of the United States House of Representatives

REPRESENTATIVE LARRY COMBEST
WORKER'S COMPENSATION & HEALTH CARE REFORM
SEPTEMBER 29, 1993

DISTRICT OFFICES

ROOM 613
FEDERAL BUILDING
LUBBOCK, TX 79401
(806) 763-1611

SUITE 205
3800 E. 42ND STREET
ODESSA, TX 79762
(915) 362-2631

SUITE 205
5809 S. WESTERN
AMARILLO, TX 79110
(806) 353-3945

SUITE 114
511 W. OHIO
MIDLAND, TX 79701
(915) 687-0926

Mr. Chairman, thank you for calling this hearing on the important issue of workers' compensation and the President's health care reform package. The skyrocketing cost of workers' compensation premiums is another straw destined to break the back of many hard-working West Texas business owners.

While the national average for workers' compensation benefits per employee averaged \$387 in 1990, Texas had one of the highest benefits costs at \$645 per employee. Because of the spiraling costs the state Legislature battled for more than three sessions trying to hammer out an acceptable system. Although the current system appears to be a major improvement, it may be declared unconstitutional. I mention this because workers' compensation--like health care reform--is an issue which everyone agrees needs fixing, but on which we just can't seem to agree on the solution.

Most would agree fraudulent claims by unscrupulous employees, doctors and lawyers can account for up to 30% of all claims. So I am grateful the administration has taken a small step in at least trying to address this issue.

Discussions have focussed on possibly merging the health portion of individual states' compensation programs into a national

health program and forming a commission to further study other reform options. While only limited details have been released, the complexity of this problem seems to result in many unanswered questions.

What would happen when full mental health benefits are covered under the Clinton health reform--would all workers be eligible for workers' compensation for so-called mental job-stress?

In Texas, I have been told by workers' compensation experts that federalizing the health component of workers' compensation would wreak havoc on management of the state system. I understand that because the health concerns and lost wages portions are so intertwined, the efficient management of such a system would almost be impossible.

I oppose efforts to nationalize workers' compensation or splitting sections of the program for the federal government to regulate. While Wisconsin has a model program, it would be a failure in Texas because of the diversity of workers and vast difference in types of employment. Lastly, a commission on Workers' Compensation was tried in the early 1970's with the results clearly stating that the states should be left to reform this system.

I look forward to today's testimony Mr. Chairman.

STATEMENT FOR
CONGRESSMAN FLOYD H. FLAKE
BEFORE THE COMMITTEE ON SMALL BUSINESS
SEPTEMBER 29, 1993

GOOD MORNING MR. CHAIRMAN AND MEMBERS OF THE SMALL BUSINESS COMMITTEE. I THANK THE CHAIRMAN FOR HOLDING THIS HEARING ON THE ISSUE OF WORKERS' COMPENSATION AND I LOOK FORWARD TO THE TESTIMONY OUR WITNESSES WILL PROVIDE.

MR. CHAIRMAN, THIS HEARING IS QUITE TIMELY AS THE PRESIDENT HAS RECENTLY OUTLINED HIS PROPOSAL FOR NATIONAL HEALTH CARE REFORM. IT IS CLEAR THAT HEALTH CARE COSTS, ACCOUNTING FOR 40% OF WORKERS' COMPENSATION COSTS, ARE POSING A DISTINCT THREAT TO THE GROWTH AND PRODUCTIVITY OF MANY SMALL BUSINESSES. THEREFORE, WE MUST EXAMINE ALL OF THE DRIVING FORCES WHICH CONTRIBUTE TO THE SPIRALLING COSTS OF WORKERS' COMPENSATION INCLUDING HEALTH CARE. WHILE SEEKING TO REVAMP OUR FAILING HEALTH CARE SYSTEM, WE MUST BE MINDFUL OF HOW THE INDUSTRY AFFECTS OTHER SECTORS OF OUR ECONOMY. IN ORDER TO ACHIEVE OUR GOAL OF PROVIDING ADEQUATE AND AFFORDABLE HEALTH CARE FOR ALL OF OUR NATION'S CITIZENS, WE MUST ENSURE THAT SMALL BUSINESSES DO NOT SHOULDER AN UNFAIR BURDEN OF RESPONSIBILITY AS THIS PROCESS UNFOLDS.

WITH THAT IN MIND, I AWAIT THE TESTIMONY OF OUR WITNESSES WHICH I HOPE WILL ILLUMINATE THE TRENDS ASSOCIATED WITH WORKERS' COMPENSATION COSTS. IN ADDITION, I WOULD ALSO HOPE THAT WE GAIN INSIGHT INTO THE POSITIVE ASPECTS OF WORKERS' COMPENSATION AND HOW WE MAY STRUCTURE A SYSTEM THAT IS BENEFICIAL FOR BOTH THE SMALL BUSINESS EMPLOYER AND EMPLOYEE.

I THANK OUR WITNESSES FOR APPEARING BEFORE THE COMMITTEE THIS MORNING AND I AWAIT THEIR VIEWS ON THIS IMPORTANT MATTER.

bsta32

STATEMENT OF CONGRESSMAN JIM RAMSTAD
BEFORE THE HOUSE SMALL BUSINESS COMMITTEE
September 29, 1993

SMALL BUSINESSES AND WORKERS COMPENSATION

Mr. Chairman, thank you for holding this hearing on workers' compensation and small businesses.

Welcome to those who have come to help us sort through this complex issue. I certainly look forward to hearing your testimony and suggestions for confronting this issue.

As we will no doubt hear in today's testimony, our system of workers' compensation has become a hopelessly distorted shadow of what it was intended to be.

At its inception, the workers' compensation system was designed to help businesses guarantee compensation to employees injured on the job. Employees gave up their right to sue for damages in return for the secure knowledge that they would be compensated for their injuries. In return, employers paid premiums into an insurance system as a sensible way to avoid costly settlements down the road.

Unfortunately, the premiums have increased so rapidly that many businesses, particularly small ones, simply can't keep up. Jobs are lost as businesses are forced to reduce the size of the workforce in order to meet costs. And companies are often forced to relocate to states with lower premiums.

The main question we need to address concerns the appropriate role for the federal government.

Each state operates its own individual workers' compensation system. Should Congress try to implement a national system? Or are the states themselves better equipped to evaluate their own needs?

I certainly look forward investigating these important issues at greater length.

Again, thank you for calling this hearing, Mr. Chairman.

OPENING STATEMENT BY CONGRESSMAN SAM JOHNSON
SMALL BUSINESS COMMITTEE, WORKER'S COMPENSATION
SEPTEMBER 29, 1993

MR. CHAIRMAN,

I WANT TO THANK YOU FOR HOLDING THIS HEARING ON
WORKER'S COMPENSATION AND ITS EFFECTS ON SMALL
BUSINESSES. ALTHOUGH THE ADMINISTRATION HAD
PROPOSED TO MELD WORKER'S COMP INTO THE HEALTH
CARE PACKAGE, ONLY THE HEALTH INSURANCE PORTION
WAS RECOMMENDED TO BE INCLUDED.

I LOOK FORWARD TO THE TESTIMONY OF EACH OF THE
PRO-BUSINESS GROUPS REPRESENTED HERE TODAY. I
EXPECT THAT WE WILL EXPLORE NOT ONLY THE IMPACT
OF COMBINING WORKER'S COMP INTO THE HEALTHCARE
PACKAGE, BUT WILL ALSO LOOK AT THE EXPENSE AND
BURDEN THAT WORKER'S COMP, UNLESS REFORMED,
PLACES ON THE BACKS OF SMALL BUSINESS.

YOU MAY BE AWARE THAT TEXAS HAS RECENTLY
REFORMED WORKER'S COMP -- AND IT APPEARS TO BE

WORKING EFFECTIVELY. I HOPE THAT WE CAN EXAMINE THE BENEFICIAL PORTIONS OF THESE PROGRAMS AND IMPROVE EACH SYSTEM TO MAKE THEM EFFECTIVE AND FEASIBLE FOR OUR NATION'S BUSINESS OWNERS.

Congresswoman Lucille Roybal-Allard
Committee on Small Business
Statement on the SBA 8(a) Program

September 22, 1993

Thank You Mr. Chairman:

I appreciate the opportunity to address some of my concerns about small and minority business development and the Small Business Administration's 8(a) Program.

I also want to welcome SBA Administrator Erskine Bowles, and Associate Director for Housing and Community Development Issues, Jacquelyn Williams-Bridgers, from the General Accounting Office.

Last week, I introduced Mr. Bowles at a gathering of some two hundred and fifty Hispanic CEO's of small businesses from around the country. Mr. Bowles discussed some of the major problems with the 8(a) program and his vision of what the SBA can and should be. He stressed his commitment to reducing the inefficiency and bureaucratic red-tape throughout the Small Business Administration which unnecessarily burden small business.

I hear from 8(a) firms in my district about the delays between 8(a) certification and the time new 8(a) firms receive their first contracts. In some cases, it takes two or three years. In other cases, companies never get contracts.

The fact is that the vast majority of contracts go to a very small number of firms. Thirty-one percent of the contracts go to two percent of the 8(a) companies. We need to do better than that.

Finally, there is concern that small businesses that fail to obtain contracts either in the competitive bidding process, or through the sole-source contracting procedure, are not given a clear explanation of why they were not successful in their bids. Without that explanation, there is no way for these companies to learn from the experience and to improve performance the next time around.

I look forward to hearing Mr. Bowles detailed explanation as to how he plans to revitalize the Small Business Administration and make it work efficiently and effectively on behalf of small business. Thank you.



NATIONAL BUSINESS OWNERS ASSOCIATION, INC.

STATEMENT OF

**MR. J. DREW HIATT
EXECUTIVE VICE PRESIDENT
DIRECTOR OF GOVERNMENT AFFAIRS
THE NATIONAL BUSINESS OWNERS ASSOCIATION**

ON

THE CRISIS IN WORKERS' COMPENSATION

**BEFORE THE COMMITTEE ON SMALL BUSINESS
U.S. HOUSE OF REPRESENTATIVES**

**ON BEHALF OF
THE NATIONAL BUSINESS OWNERS ASSOCIATION**

SEPTEMBER 29, 1993

Mr. Chairman and Members of the Committee, my name is J. Drew Hiatt, and I am Executive Vice President and Director of Government Affairs for the National Business Owners Association. We appreciate very much the opportunity to present our views on the growing crisis in the national workers' compensation system and to examine with you both the scope and severity of this problem as well as its effect and burden on America's small business owners. Furthermore, we welcome the opportunity to discuss the Clinton Administration's proposal to integrate the medical portion of workers' compensation with its health care plan and to offer our perspective and comments on this proposal.

The National Business Owners Association represents nearly 8,000 small business owners, and has an active and rapidly expanding membership. Its philosophy is based on the belief that a vibrant and robust private sector and a strong and competitive free enterprise economy are essential to create and increase economic growth, opportunity, jobs, and prosperity for all Americans. NBOA vigorously represents the interests of its members before Congress as well as federal, state, and local government. It also works to influence and enact national policies that promote economic growth and entrepreneurship. As part of its efforts to advocate and adopt beneficial laws and regulations, NBOA consistently communicates the concerns and legislative priorities of business owners to lawmakers, government officials, the public, and the media.

We commend you, Mr. Chairman, for your leadership in convening this hearing today to address the growing problem and horrendous burden of skyrocketing workers' compensation costs on small business. Our members and other small business owners across the country are profoundly concerned about soaring workers' compensation premiums and the pressure they continue to exert on their bottom lines.

Mr. Chairman, America's workers' compensation system is not in a state of crisis, it is in a state of chaos. It has become increasingly clear that the underlying purpose of workers' compensation has been lost. In the 82 years since it was first established, the nation's workers' compensation system has strayed so far from its original purpose that it has become something it was never intended to be. It no longer serves the employees and employers it was designed to serve. Fraud and abuse, spiralling medical costs, legal activism, and judicial expansion of compensable benefits have conspired to ruin what was once a progressive and balanced system.

Small business owners are crying out for relief from the crushing burden of exorbitant workers' compensation premiums. These costs now represent the single fastest growing labor cost. For those not directly subject to the shock of steadily rising premium rates, what is happening in workers' compensation may only be characterized as an emerging crisis, but to those who are directly exposed to the full brunt of these costs, it is a catastrophe in full swing. Escalating workers' compensation premiums are gripping small business owners by the throat. Many have been strangled already, more are certain to be. As a result, small

business owners are no longer struggling for success. Their goal is more basic. They are struggling for survival. And they are worried about whether and how long they can survive if there is no respite from mounting workers' compensation rates.

If labor costs -- particularly workers' compensation premiums -- continue to rise beyond small business owners' ability to pay them, how much longer will it be before the real consequences of these costs are measured in massive job losses? Small business is America's leading employer. Today, six in 10 Americans take home a paycheck from a small firm. Small businesses also create all our new jobs. In fact, they are expected to create more than three-quarters of the 43 million new jobs needed over the next 25 years. Unless we do something soon to relieve the pressure of these high labor costs on small business owners, we will face job losses. This will only hurt healthy workers by taking away their jobs and injured workers by taking away medical care and lost wage benefits. We cannot help employees by driving their employers out of business.

The short-term and long-term implications and consequences of escalating workers' compensation costs for the continued vitality, well-being, and productivity of our entrepreneurial sector are far-reaching and dire. Many states' economies also simply handle the unabated escalation of workers compensation costs. As these costs balloon, employers begin to consider relocating to lower-cost states. This contributes to widespread economic upheaval that is registered in many ways: lost jobs, lost investment, and lost revenue. States, small business owners, and workers are not the only ones who lose because of higher

workers' compensation costs. Consumers also lose when these costs are passed on in the form of higher prices. And taxpayers also lose by paying higher taxes to cover local, state, and federal employees.

The workers' compensation system must be reformed to restore it to its historical purpose: a set of laws intended to benefit both employee and employer. We look forward to working with you and the Members of this Committee to develop a meaningful and workable solution to the daunting challenge of providing small business owners relief from the spiralling costs of workers' compensation. Together, we can lay the groundwork for fundamental change in the workers' compensation system and return it to its original purpose as we strengthen and improve it in the process.

THE HISTORY AND PURPOSE OF THE WORKERS' COMPENSATION SYSTEM

The workers' compensation system is America's oldest social insurance program. Since its inception more than 80 years ago, it has served employees and employers alike, functioning as an exclusive remedy for work-related injuries and illnesses. Through no-fault insurance, employers pay the medical expenses and lost wages for employees who are injured or become ill on the job until they can return to work. In exchange for this pledge, employees relinquish their right to sue employers for medical and disability benefits. If employees are permanently disabled, their benefits are not subject to taxation. In the event of

death resulting from a job-related accident, injury, or disease, workers' benefits go to survivors.

Wisconsin was the first state to enact a permanent workers' compensation law in 1911. By 1949, all 50 states and the District of Columbia had established similar systems. Today, all 50 states operate separate systems, administering workers' compensation laws for and on behalf of employees and employers.

During the 1950s and 1960s, workers' compensation costs were low largely because disability benefits lagged behind inflation. In 1970, President Nixon, in responding to growing criticism of the workers' compensation system, appointed a national commission to recommend reforms. The commission encouraged Congress to impose national standards for workers' compensation upon those states that did not increase benefits for employees or adopt various administrative standards. Fearing Congressional action to impose national standards, states quickly responding by boosting benefit levels significantly. Employers, particularly small employers, saw their workers' compensation premiums rise through the 1970s and early 1980s because of these state-mandated benefit increases.

THE COST EXPLOSION IN WORKERS' COMPENSATION

Today, 96 million American workers — about nine of every ten — are covered by workers' compensation. Nationwide, job-related injuries and illness in 1991 cost public and

private employers an estimated \$62 billion in workers' compensation expenditures. This amount is up from \$56 billion in 1990. This rapid escalation is especially dramatic considering the fact that in 1980 the cost was \$22 billion, in 1970 less than \$5 billion and in 1960 slightly over \$2 billion. In a decade, workers' compensation outlays have nearly tripled and over the last 30 years they have exploded.

Over the past decade, even though the Consumer Price Index rose at an annual rate of slightly more than 5 percent, indemnity benefits have escalated by nearly 300 percent, or almost 15 percent annually. Medical expenses have risen even faster — 374 percent since 1981, or a yearly average rate of nearly 17 percent. Premium costs have naturally reflected these increases. The Workers' Compensation Research Institute estimates that the cost of workers' compensation will reach \$70 billion this year, making it the fastest growing labor cost. The current trend in the alarming growth rate of workers' compensation costs does not portend well for small business owners. Based on the present rate, these costs will triple by the year 2000.

THE ROOT CAUSES OF SOARING WORKERS' COMPENSATION COSTS

The factors that contribute to the soaring costs of workers' compensation insurance are fraud and abuse, unrestrained medical costs, excessive legal disputes, and judicial expansion of compensable benefits. Small business owners are demanding relief from the crippling costs of ever-increasing workers' compensation premiums. They recognize the threat such

costs, if left unchecked, pose to their own businesses and livelihoods as well as to economic development, productivity, employment, and job creation.

Fraud and Abuse

Insurance specialists from various states believe that workers' compensation fraud is a factor in up to 30 percent of all workers' compensation claims. The system is plagued by fraudulent and exaggerated claims. Yet it is often difficult to combat fraud and abuse primarily because it is difficult to prosecute fraudulent claimants. When caught, although future benefits are terminated, typically even the most flagrant offenders escape criminal punishment. While the cessation of benefits is a major victory for the payer of the claim, it does little to deter others from pursuing fraudulent and exaggerated claims. Claimants are often not the only party to workers' compensation fraud; certain unscrupulous employers, doctors, lawyers, chiropractors, insurance agents, suppliers, and others are participants as well. The section below highlights some of the more common fraud schemes perpetrated by dishonest individuals.

Workers' Compensation Premium Fraud Schemes

Forged Documents

Sometimes contractors or subcontractors will unlawfully fail to secure the

payment of workers' compensation claims, but will seek to forge or alter prior certificates showing coverage to collect payment for work done or show proof of coverage to authorities. In addition to felony charges for the workers' compensation in fraud, cases may also be made for forgery, false official statement, and theft.

Understatement of Payroll

Employers may submit statements of payroll which represent only a portion of the actual employee force, or estimates of payroll which fall short of payroll already being paid are often submitted to reduce workers' compensation premiums.

Misclassification of Employees

Employers may report large numbers of employees in categories which carry a lower premium rate.

Corporate Gerrymandering

The assigned risk pool will accept employers with poor loss experience, but it will not accept any employer that owes premiums to an insurer from an earlier audit. Some employers or employee leasing operations that owe premium will create a new corporate entity in an attempt to obtain coverage through misrepresentation. An

additional reason for a "new" corporation is to avoid higher premiums caused by experience modifiers due to heavy losses. The proper reaction by an employer to a higher premium due to experience should be to take steps to make operations safe and avoid employee injuries. Some employers choose to misrepresent their history to lower their premiums. This misrepresentation is now a felony.

Agent Schemes

Although most agents are reputable, some unscrupulous agents may pocket premiums or use high-pressure tactics to gain a large commission. Two of the more common agent schemes follow.

Pocketing Premiums

In pocketing schemes, an unscrupulous agent issues a certificate indicating the customer is insured against specific losses but never forwards the customer's premium payment to the insurance company.

Conspiring to Reduce Premiums

Sometimes an agent, in an attempt to retain a client by obtaining the lowest

premium, will either alter the application submitted by an employer, or advise the employer incorrectly on the meaning of entries. In either case the result is an application that misrepresents the coverage actually required. Even though the employer may not be fully aware that the application is in violation of the law, his signature on the form may bring him into a conspiracy to obtain lower premiums unlawfully.

Some agents will recommend to an employer schemes which they think will "circumvent" the law. An example is transferring the employees from an employer with a high experience modified premium to an employee leasing operation with the specific purpose of avoiding the experience modifier. Others will recommend that employers "fudge" on payroll estimates or the actual job classifications of employees.

In either of the above scenarios, both the employer and the agent are subject to criminal prosecution for the conspiracy.

Workers' Compensation Claim Fraud Schemes

Injury Fraud

In this scheme, what usually begins as a minor injury on the job develops into

a golden opportunity for an early retirement, a paycheck without having to work, or an income supplement from an insurance company.

Here, false information is presented to the workers' compensation carrier. The report describes the claimant as totally or partially disabled and either unable to work at all, or only able to work part-time. In many cases those schemes are enhanced with the assistance of an unscrupulous doctor who, for an extra fee, provides a false diagnosis of the claimant's condition and fabricates medical records for phony treatments.

Double Dipping

Claimants have collected workers' compensation benefits and worked full- or part-time on another job, often under an alias.

Lawyer/Doctor Schemes

This scheme usually requires three key players to be successful: A lawyer, a "capper", and a doctor.

The Lawyer

The lawyer is usually the prime mover in the scheme. Whether the case involves altogether phony or greatly exaggerated injuries, it is the lawyer who profits most in nearly every case. Most workers' compensation cases are accepted by personal injury lawyers on a contingent-fee basis. This means the lawyer and the client agree that the fee will be based on a percentage of the settlement or court award in the case. If no settlement or court award is made, the lawyer will not be paid.

To operate a law practice exclusively in this manner requires a high volume of cases to insure a steady cash flow. It follows that the higher the settlement, the higher the reward. Lawyers running personal injury mills, as they are called, are not eager to engage in litigation. They rely on the insurance company's desire to settle quickly, realizing the expense a company must absorb by going to court to fight any claim, even a frivolous one.

Lawyers will usually attempt to entice a victim to cooperate in the scheme by promising a big "payday" from the insurance company. The big payday often never arrives for the victim, since medical fees, runner fees, and contingency fees may be deducted before the victim gets his or her share. Some lawyers blatantly rip-off their clients by forging the signature of the victim on the insurance company check. Even if these victims discover they were cheated by their lawyers, they are reluctant to report fraud, since they too conspired to defraud the insurance company.

The "Capper"

To build their clientele, some lawyers and often doctors use "cappers" to entice persons in unemployment lines to become clients or patients. The capper may be paid a flat fee or a percentage of the final take. Whether the capper approaches the victim at the worksite or later, workers' compensation fraud schemes often begin with this contact.

The Doctor

In most phony or inflated personal injury cases, the best way to lend authenticity to the scheme is by finding a doctor who will prescribe unneeded treatments. The doctor can cause medical expenses to escalate quickly and fuel the desire to settle, even if the claim is suspicious. A doctor working in collusion with a lawyer and one or more runners may collect a prearranged fee for a false medical report, or will actually prescribe unnecessary treatments for accident victims and collect a usual per-visit fee from the insurance company.

Even in cases with real injuries, some doctors grossly inflate the number of treatments normally prescribed. Victims of minor accidents have submitted claims for more than 40 doctor visits. Most allegedly involve some form of physiotherapy, such as heat packs, diathermy, or ultrasonic treatments.

Some unscrupulous doctors may charge for visits never made by the accident victim then split the insurance payments for the non-visits with the lawyer.

The Hospital/Clinic, etc. Employee

In some cases the conspiracy will also involve the participation of a hospital or clinic employee who will allow the use of facilities in a scheme to fraudulently violate the workers' compensation law.

Unrestrained Medical Costs

Medical cost containment is a major challenge facing workers' compensation systems. Overall, medical costs represent, on average, more than 40 percent of total workers' compensation costs, according to a national survey conducted by the Workers Compensation Research Institute in 1991. In certain states, these costs may exceed 60 percent. Since workers' compensation pays for all medical care, many health care providers have made excessive use of the system. According to a report prepared by the Office of Management and Budget (OMB), "health providers know that workers' compensation recipients are not sensitive to the price of medical services and therefore they can charge more to the employers for these services." OMB cited a study finding that, on average, health care providers charge more than twice as much for workers' compensation treatments as they do for comparable off-work injuries.

In particular, there is concern that ownership by physicians of medical facilities to which they refer patients leads to overuse of such facilities. A study published in *The New England Journal of Medicine* found that workers' compensation medical cases were referred for treatment more often, and at a higher cost, by physicians who owned facilities. Specifically, physical therapy was initiated 2.3 times more often by self-referring physicians. The mean cost of psychiatric evaluation was higher when recommended by self-referring physicians. And 38 percent of the MRI scans requested by self-referring physicians were found to be medically inappropriate, compared to 28 percent requested by physicians referring patients to independent facilities.

Substantial efforts by all participants in the workers' compensation system are necessary to slow the rapid growth of medical expenses.

Rising Legal Costs

An OMB study found that costly litigation often results from disputes over whether claims are in fact related to the workplace. Litigation has become a common avenue to secure benefits that a claimant may not otherwise be entitled to receive under state law as a result of a job-related injury or illness.

In addition to fraud by some employers and employees, many lawyers and doctors have exploited the workers' compensation system's vulnerability. A study by two economists

at the State University of New York in Buffalo has found that during recessions, fewer billing hours elsewhere lead to increased involvement of lawyers in workers' compensation cases. This increased litigation drives up costs through inflated indemnity payments, which may include reimbursement of the claimant's legal fees, as well as the cost of attorneys, doctors and expert witnesses on the part of the insurer.

Judicial Expansion of Compensable Benefits

Both the courts and state commissions have broadly expanded the definition of what constitutes a compensable injury or illness. In doing so, they have contributed directly to the creation of new benefits to which claimants may be entitled. The indemnity cost per case has risen nearly 200 percent since 1981, averaging an 11 percent increase each year. Indemnity benefits are generally a function of the injured worker's wages; however, since 1981, average weekly wages have grown by only 4 percent a year. The additional growth in indemnity costs is the result of the broadening definition of compensability as well as the increasing involvement of lawyers in what was originally intended to be a no-fault system. While court decisions and commission rulings help create opportunities for additional benefits for workers and new fees for doctors and lawyers, they seldom take into account the increased burdens and costs for small business owners that arise from such actions.

ACTUAL WORKERS' COMPENSATION CASES

To illustrate some of the problems discussed above, below are examples of actual workers' compensation cases. The names of the claimants have been changed to protect their identity, but the facts surrounding each case have not been altered in any way.

James Dawson

James Dawson of North Carolina is a truck driver who was pinned between two vehicles and suffered trauma to his chest. His physician diagnosed him with esophagus reflux and indicated that Mr. Dawson would be unable to work in any capacity for at least one year. In addition, the doctor said, the claimant would need extensive medical treatment for rehabilitative purposes, vocational training as the claimant would not be able to return to his previous occupation, and possible future surgery.

By assigning surveillance the insurer was able to determine that Mr. Dawson was engaging in activities which exceeded the restrictions supposedly keeping him from returning to his employment.

A form was filed with the North Carolina Industrial Commission and the investigative report and video tape were used to terminate compensation payments. Despite this successful effort, the insurer still had to pay for nearly \$50,000 in indemnity and medical benefits in addition to a settlement.

Joe Evans

Joe Evans of North Carolina was in an automobile accident and sustained a lacerated finger, multiple contusions, left wrist sprain, cervical strain, and fractured bones in his face. His physicians indicated that he would need diagnostic testing to rule out disc herniation and possible reconstructive surgery to his cheek.

Despite the physician's report, investigators found Mr. Evans playing golf on a regular basis, often more than one game a day. However, this strong evidence was not enough for the insurer to avoid paying nearly \$8,000 in medical, indemnity, and other benefits.

Mark Horn

Mark Horn claimed he injured his back while working for his employer on a farm. Doctors determined that Mr. Horn would need surgery to correct the problem. The insurer was able to determine that the claimant had actually hurt his back while working for another company, and videotaped the claimant lifting a moped without difficulty. With this information, the claim was denied, however, not before the insurer spent nearly \$2,000 in medical, indemnity, and other benefits.

Leroy LaRue

Leroy LaRue of Louisiana alleged that he fractured his elbow while drilling. He then complained of shoulder and neck problems, which his doctor related to the most recent injury. Discussions with the employer, the claimant and his wife revealed conflicting stories. A background check and surveillance were ordered. The check showed that Mr. LaRue had three outstanding suits for injuries, and surveillance showed that he was working on the side with no evident disability. Despite this finding, the insurer had to pay out nearly \$9,000 in benefits.

Ed Hughes

Mr. Ed Hughes, a cement finisher, was injured while he was pumping concrete. A steel boom swung around hitting the overhead power lines, resulting in electrical shock to Mr. Hughes and causing a temporary loss of consciousness.

Upon admission to the hospital, Mr. Hughes tested positive for cocaine. Because of this positive test, the insurer thought it would be responsible for the initial medical cost only. Because of attorney involvement, it was later determined that the positive testing was not a contributing factor in the incident. The insured did not have a written drug policy in force, therefore, the insurance company was obligated to accept compensability.

Mr. Hughes continued to complain of body pain and headaches, and was subsequently evaluated by many different doctors, including an ophthalmologist, orthopaedist, neurologist

as well as a neuropsychiatrist. No objective physical findings confirmed these continued complaints.

Surveillance videos showed Mr. Hughes capable of climbing over railway cars, running, jumping, and walking over seven blocks to his residence, all without apparent discomfort. Confronted with the videotape, the claimant's complaints changed from physical disabilities to psychological problems including decreased appetite, depression, and crying spells. Incredibly, the insurer remains required to pay benefits to this claimant, and has spent in excess of \$23,000 to date.

Truck Driver

A truck driver working for a small company suffered a minor head injury. The claimant alleged continuous subjective symptoms, and his physician refused to release him to return to his normal occupation for nearly a year. As the claimant had no objective findings to support his allegations of continuing disability, surveillance was assigned. After two unsuccessful attempts, the insurer proved that the claimant was capable of driving and in fact was transporting race cars without the knowledge of his physician. On the basis of the investigation, payment of temporary disability benefits was stopped and the treating physician released the claimant with no permanent partial disability rating. This fraudulent claim ended up costing more than \$23,000.

Truck Driver

A 37-year-old truck driver alleged that he injured his knee when he attempted to redistribute a load. Investigation revealed that the injury occurred while the claimant was off-log and that the claimant had altered his logs in an attempt to bolster his compensation claim. Although he claimed to be disabled, he was playing golf on a regular basis. Voluntary payment on the claim was refused, but the insurer was required to defend this position in litigation. The insurer prevailed in court, but the cost to defeat this fraudulent claim was nearly \$7,000.

Painter

A painter who had worked for a small cabinet company for all of two weeks violated company policy and safety warnings by playing with a butane lighter in an area clearly designated as harboring flammable substances. The lighter ignited a bucket of paint thinner. As other employees ran to get fire extinguishers, the painter, ignoring requests that he not touch the bucket, picked it up and began to run it outside. This caused the flames to engulf the young man's head and body, ultimately leading to 29 percent total body surface area burns, including third-degree burns and skin destruction of the arms, chest, and face. This accident, which arose from a violation of company policy and safety rules, was considered compensable. The total cost to resolve the claim was nearly \$200,000.

Mr. Alan Johns

Alan Johns is a delivery helper who was injured when he was helping another employee deliver a washer/dryer to a customer home. While carrying this appliance down a flight of stairs, he felt pain in his back. He was treated with physical therapy and medication and returned to work.

Later, while picking up a refrigerator, he claimed injury to his left shoulder and was treated by the same physician. The diagnosis was cervical and lumbar strain. After much more therapy, medication, and testing, Mr. Johns remained off work. Even though the claimant was videotaped throwing objects from a Mardi Gras float on which he stood for at least eight hours, his physician refused to return him to work, claiming that it was simply one of Mr. Johns' better days and resulted from the amount of medication taken.

Mr. Johns is a high school graduate and is certified as a bartender. Due to the efforts of his attorney, and a treating physician willing to order endless testing, there is no anticipation of his return to gainful employment. To date, this claim has cost a total of nearly \$23,000 in indemnity, medical, and other related expenses.

STATES TAKE AIM AT WORKERS' COMPENSATION REFORM

In recent years, states have responded more aggressively to the demand of small businesses for relief from the high costs of workers' compensation. States recognize that these costs impose a tremendous burden on small firms. Concerns over the effect of these horrendous costs on the continued health of the small business sector and its ability to fuel economic growth and create jobs are driving many states to take action. Many states are now in the forefront of efforts to enact reform, and workers' compensation laws have seen changes in many states. Other reform initiatives are under way in other states. However, without tough anti-fraud laws, many states are not ready for the challenge.

Oregon Gets Tough on Claims Cheaters

Perhaps the most successful war against workers' compensation fraud has been waged by Oregon. From 1984 to 1987, it had the highest frequency of claims of any state, with one in four estimated to contain some element of fraud. The pervasive fraud and abuse, dramatized by a few celebrated cases, incensed the public. Finally, the Oregon legislature, prompted by then-Governor Neil Goldschmidt, enacted a landmark reform package in 1990.

The State Accident Insurance Found (SAIF), a quasi-government corporation that underwrites the state's largest share of workers' compensation business, launched a comprehensive anti-fraud campaign. Undercover and surveillance units were set up. After the crackdown, the percentage of disability claims rejected by SAIF increased from 12 to 29 percent. Most important, the number of claims filed dropped by 23 percent.

State officials helped the reform process by launching well-publicized anti-fraud efforts and encouraging the private sector to create on-the-job safety and back-to-work programs. As a result, Oregon now has a declining injury, illness, and fatality rate among its workers. The state also reduced its premiums by 12 percent in 1991 and by another 11 percent in 1992.

Florida Task Force Targets Fraud

Florida is increasing its crackdown on workers' compensation offenders. This ranges from the claimant who fakes an injury before being fired or laid off to the business owner who documents a smaller payroll to reduce premiums.

A task force composed of representatives of insurance companies, employers, and insurance regulators is working to combat fraud. It is compiling examples of fraud and plans on publicizing cases of people who got caught. The panel is also contemplating starting a toll-free number for Floridians to report suspected cases of abuse.

During 1991 the Florida Department of Insurance started a workers' compensation fraud bureau. Seven investigators are currently working on approximately 150 pending cases. Under Florida law, workers caught defrauding the workers' compensation system can be charged with third degree felony, which could result in a sentence of five years or a \$5,000 fine.

Maryland Enacts Reforms to Roll Back Premiums

Maryland Governor William Donald Schaefer appointed a similar business/labor committee in 1987 to craft what became a major reform bill in that state. The legislation in Maryland produced four consecutive years of premium reductions.

SMALL BUSINESS OWNERS SEEK THEIR OWN SOLUTION IN FORMING GROUP SELF-INSURANCE FUNDS

Small business owners have tried to cope with the growing burden of workers' compensation costs as they search for sensible solutions. The National Business Owners Association has found in the concept of group self-insurance funds a more cost-effective alternative to traditional workers' compensation insurance. It is one that provides small businesses with substantial relief from the soaring and crippling costs of such insurance and the additional financial burdens it imposes. If small business owners are to remain competitive, they must cut costs and reduce overall pressure on their bottom line.

NBOA sponsors the formation of group self-insurance funds. These funds are established to assist small business owners in controlling the costs associated with their workers' compensation coverage. In essence, these funds are similar to mutual insurance companies. A self-insured group is formed by employers (in this case, small business owners) that are, in most instances, in the same or similar business. These employers are

like-minded to the extent that they are willing to change past behaviors in dealing with injured workers. They are also willing to accept the liabilities for losses of the group in excess of their loss fund pool. However, through efforts to prevent accidents by implementing workplace safety programs, provide managed care/disability management, and reduce loss costs, these aggressive claim management employers will share financially in the group's success. Group self-insurance is an economically viable alternative to the conventional insurance market. In recent years, self-insurance groups have given employers the empowerment and the incentive to do something about the crisis in workers' compensation insurance. Moreover, these self-insurance funds are a powerful tool for controlling medical costs more effectively.

RECOMMENDATIONS FOR REFORMING THE NATION'S WORKERS' COMPENSATION SYSTEM

As a first step toward reforming the nation's workers' compensation system, we would recommend introducing and passing legislation to establish a national, bipartisan commission to examine the current workers' compensation crisis. Such a commission would be comprised of representatives from business, particularly small business, labor, insurance, medicine, law, consumer groups, federal, state, and local government, as well as other concerned groups.

The purpose of the panel would be to develop recommendations and to create national guidelines for states to follow in enacting broad-based reforms of workers' compensation laws. A further goal would be to ensure that the system is returned to its historical roots and intended purpose as one that serves both employees and employers. We believe this commission would provide a national forum in which to explore the current crisis and offer a platform for reform.

By moving this legislation, this Committee would signal its resolve and commitment to tackle the problem of workers' compensation. This Committee can play an important role as a catalyst for encouraging dialogue, information exchanges, and cooperation among the parties as they work toward meaningful and substantial reform in the system.

We would not recommend nor favor at this time legislation to craft a national workers' compensation law. Such a law would be construed as an encroachment upon the traditional rights and responsibilities of states in the adoption and administration of workers' compensation laws. The commission would help obviate the need for national legislation to preempt state jurisdiction in the passage and administration of such laws.

THE CLINTON ADMINISTRATION'S PROPOSAL TO INTEGRATE THE MEDICAL PORTION OF WORKERS' COMPENSATION INSURANCE WITH THE HEALTH CARE PLAN

The Clinton Administration plans to restructure the workers' compensation system as part of its health care reform plan. Rising costs are being fueled by runaway medical spending, and President Clinton wants to stem these costs. He announced he will propose folding the medical portion of workers' compensation into his new national health care program, while leaving wage indemnity and disability management responsibilities to the states. To prevent safety-conscious businesses from subsidizing more dangerous workplaces, OMB expects that employers will pay combined health and workers' compensation premiums based on their past workers' compensation payments.

OMB envisions that the new program would be phased in gradually as other components of health reform are adopted. Initially, worker's compensation health benefits would be integrated with health insurance benefits only in situations where there is existing employer-based health coverage. When health reform is fully implemented and health coverage for all employees is mandated, all workers' compensation health benefits will be merged with the new national health care program.

The President maintains that the integration of workers' compensation and health insurance will result in savings for businesses by eliminating overlapping programs. Hillary Rodham Clinton, who chaired the now-disbanded White House task force on health care reform, has noted that this reform would bring efficiency and savings to a high-cost area that is especially burdensome to small companies. In addition, OMB expects the emphasis on managed care in the Administration's health reform plan to encourage employees to seek

health care that is appropriate for the illness, rather than use medical "experts" for litigious purposes. Workers' compensation reform would also prevent health care providers from charging more for workers' compensation cases. OMB also hopes that the reform proposal would reduce "frivolous and aggregated" workers' compensation claims. The President has warned, however, that safeguards must be enacted to prevent employees from abusing a new system.

According to OMB, most large employers and many labor unions support combining employer-provided health insurance and workers' compensation health benefits, hoping that it would be simpler and more workable than the current system. Critics charge, however, that separating workers' compensation into wages and medical care components would make the system more complicated without necessarily resulting in cost savings. In addition, many insurance companies argue that they need to retain control over claims to effectively control costs. Such a change would also involve the federal government in an area traditionally left to the states.

The National Business Owners Association opposes the Administration's proposal to merge the medical portion of workers' compensation with the health care plan. It must be understood that workers' compensation is much more than a medical delivery system; it is an overall workplace disability management system which focuses on achieving maximum medical improvement. Its goal is to ensure that injured workers return to their jobs as quickly as possible.

We have serious reservations about an integrated approach. First, we believe that this approach would lack the incentives to tailor medical programs for injured workers. Second, we are concerned that this might lead to a relaxed attitude toward workplace safety at some companies. Under an integrated approach, employers with good workplace safety records would subsidize employers with poor records. This would be unfair.

Cost shifting. Workers' compensation provides a package of medical benefits. In contrast to most health insurance plans -- which feature annual and lifetime dollar limits, employee premium contributions, employee deductibles and co-payments, and exclude certain treatments -- workers' compensation offers injured workers virtually unlimited medical care, with no "out-of-pocket" expenses to them. To the extent that the national health plan would impose restrictions on benefits for nonwork-related injuries and illnesses, it will encourage cost shifting and higher costs for work-related treatments.

Cross subsidies. Workers' compensation is designed to apply maximum economic pressure to achieve workplace safety. The standard National Council on Compensation Insurance experience rating modification plan, mandatory for qualifying employers, focuses this economic pressure by connecting the premium paid by individual employers to their records of losses. Community rating, which does not target such incentives on individual employers, will weaken the safety incentives of the current, cost-based pricing system.

Capitation-based reimbursements. The American health care system generally operates on a fee-for-service basis. This approach creates incentives to increase both the frequency and the cost of services. These incentives are even greater when the patient has little or no out-of-pocket expenses to consider. Under the fixed fees of a capitation-based system, the economic incentives may tend to promote more conservative methods of treatment that minimize the provider's time and costs. This implies longer periods of disability which, in turn, will mean longer-lasting workers' compensation disability payments and higher costs.

Pay-as-you-go financing. There are indications that the national health care plan will operate on the annual treatment basis common to other health plans. This is in sharp contrast to workers' compensation, which covers all treatments, regardless of when delivered, arising from accidents occurring during the period covered by the policy. On the average, 80 percent of workers' compensation medical costs are incurred after the first year of payments. Pay-as-you-go financing would postpone recognition of these costs and lead to the buildup of significant unfunded liabilities.

Claims management. By splitting workers' compensation coverage into indemnity (wage replacement), which would continue to be covered as it is today, and medical, which would be handled by a different entity, claims management of the indemnity coverage may be weakened. Studies have shown that when employers lose control of the medical component, as is likely in any integrated program, wage replacement costs go up.

Even if the economic incentives for conservative treatment can be balanced with the need to return workers to work (and limit indemnity costs), the investigation and resolution of work-related issues are likely to be coordinated. The resulting delays in determining indemnity benefits and in reaching maximum medical improvement and certification for return to work will extend the duration of disability payments. Moreover, overcoming these obstacles may require higher administrative expenses.

Exclusive remedy. The question of how integrating workers' compensation into the national health insurance plan will affect the exclusive remedy provision of workers' compensation must be addressed.

If the medical component of workers' compensation is moved into a national health system, someone must still pay for the benefits. Shifting costs from one system to another does not make them go away.

The National Business Owners Association asked its members in an August 1993 survey on health care reform whether they would favor including the medical portion of workers' compensation in the Administration's new health care reform program. Respondents strongly opposed the proposal.

Whatever direction or shape the final proposal or legislation might take, we believe it is important for the Administration, the Congress, and this Committee to recognize the value

of self-insurance to the American small business community and to ensure that this concept is not only preserved but that the status of existing self-insurance funds is maintained on behalf of small employers and their employees.

CONCLUSION

The National Business Owners Association appreciates this opportunity to offer our views on the workers' compensation crisis and the Administration's proposal to fold the medical portion of workers' compensation into its health care plan. We will carefully examine any proposal to integrate these two components and would urge thoughtful consideration of the arguments we have made in regard to the Clinton Administration's proposal. Mr. Chairman, we look forward to working with you and the Members of this Committee over the coming months to achieve meaningful reform of the nation's worker's compensation system, to restore it to order, and to return it to the system it was intended to be: one that benefits employees and employers alike.

TESTIMONY ON WORKERS' COMPENSATION AND MEDICAL BENEFITS

TO THE
COMMITTEE ON SMALL BUSINESS
OF THE HOUSE OF REPRESENTATIVES
CONGRESS OF THE UNITED STATES

BY
JOHN F. BURTON, JR.
DIRECTOR, INSTITUTE OF MANAGEMENT AND LABOR RELATIONS
AND
ACTING DEAN, SCHOOL OF BUSINESS - NEW BRUNSWICK
RUTGERS UNIVERSITY

SEPTEMBER 29, 1993

Chairman LaFalce and Members of the Committee on Small Business of the House of Representatives, I am pleased to testify at your request on the issue of workers' compensation. I will specifically discuss recent developments in the costs of workers' compensation, the role of medical benefits in those cost trends, the sources of the higher medical costs and possible solutions to those higher costs, and the pros and cons of integrating the medical component of workers' compensation into a national health insurance plan.

Recent Developments in the Costs of Workers' Compensation.

Preliminary data for 1992 indicate that nationally the employers' costs of workers' compensation reached \$60 billion. Over recent decades, these costs have soared. In 1960, the national costs were \$2.1 billion; costs then increased to \$4.9 billion in 1970, \$22.3 billion in 1980, and \$53.1 billion in 1990.

The employers' costs have increased much more rapidly than payroll over this period. In 1960, workers' compensation costs as a percent of payroll were 0.93 nationally; by 1970, the figure was 1.11 percent; by 1980, 1.96 percent; and by 1990 costs to employers averaged 2.36 percent. Preliminary data for 1992 indicated that the national average cost of workers' compensation to employers was 2.5 percent of payroll.

These costs vary considerably among states, with employers in high cost states such as California and Montana spending more than three times as much on workers' compensation as comparable employers in Indiana or Utah. There are also variations within

states, with manufacturing industries typically spending twice as much on workers' compensation as a percent of payroll as other industries. Even within industries, there are substantial differences in workers' compensation costs as a percent of payroll due to the effect of experience rating, which charges higher premiums to firms with higher benefit payments.

Small firms are covered by the workers' compensation programs in most states, although about 15 states exempt employers with a limited number of employees (typically three or fewer employees). Nationally about 87 percent of the workforce is covered by workers' compensation, although coverage is less than 75% in Tennessee, Louisiana, and Texas. Costs for small employers vary among states and industries, but there is no evidence that small employers generally pay more than their fair share of the costs of the program.

Reasons for the Higher Costs of Workers' Compensation.

The sources of the higher costs of workers' compensation have varied through time. During the 1970s, the primary source was the higher statutory levels of cash benefits enacted by the states in order to provide adequate benefits for injured workers. Since the early 1980s, a primary source of higher costs has been escalating medical benefits. For example, between 1984 and 1990, expenditures on medical benefits increased 15.6% a year, much higher than the annual increase in expenditures on cash benefits of 10.8%.

As a result of these disparate growth rates in expenditures, medical benefits increased their share of all workers' compensation

benefits from 35.0% in 1984 to 40.9% in 1990. Between 1990 and 1991, expenditures for medical benefits slowed from previous years (up 10.9%), but still grew faster than cash benefits (up 10.7%), and so by 1991 medical benefits accounted for 41.0 percent of all workers' compensation benefits payments - the higher percentage at least since 1960 and probably the highest share in the 80 year history of workers' compensation.

Not only are medical expenditures in workers' compensation increasing more rapidly than workers' compensation cash benefits, they have also outpaced the growth in medical expenditures in the U.S. general health care system in every five-year period since 1975. The greatest disparity was from 1985 to 1990, when health care expenditures nationally went up 9.5% a year, while workers' compensation health care expenditures went up 15.2% a year.

(From 1990 to 1991, workers' compensation health care expenditures were up 10.9 percent while national health care expenditures were up 11.4%. It is too soon to celebrate the "victory" in workers' compensation, however, since the slow growth of employment from 1990 to 1991 probably was a temporary depressant to workers' compensation medical cost increases.)

The Reasons for the Higher Medical Costs: the First Level of Explanation.

There are two elementary reasons why workers' compensation medical costs are a problem: price and quantity. A study in Minnesota indicated that charges for identical or similar medical services were more than twice as high for injured workers receiving

workers' compensation medical care as for similar workers receiving medical care through the Blue Cross program. The same study found that workers' compensation patients typically received a greater quantity of services than did Blue Cross patients with similar injuries.

The Reasons for the Higher Medical Costs: the Second Level of Explanations.

The workers' compensation program appears to provide a larger quantity of health care services and to charge more per unit of service than other parts of the U.S. health care system, and apparently the quantity and/or the charges have been increasing more rapidly than the other parts of the health care system during most of the last twenty years. What explains these developments? Part of the answer appears to involve health care providers, part the patients, part the delivery system, and part the payers.

Providers. The general health care system has been increasingly subject to approaches designed to limit the quantity and price of services delivered by health care providers. These approaches include the increasing prevalence of health maintenance organizations (HMOs) for basic health care and the diagnostic related group (DRG) method of reimbursing hospitals, both of which provide financial incentives to health care providers to limit the amount of health care provided. Further, utilization review by major insurers has limited the quantity of services for which providers can successfully bill.

In addition, the traditional fee-for-service method of

reimbursing providers, in which little control was exercised over the charges for medical services, has been increasingly replaced by fee schedules, such as those imposed by the Medicaid program, and by the use of preferred provider organizations (PPOs), which channel patients to providers who offer lower charges.

These cost containment approaches directed at health care providers are less prevalent in the workers' compensation programs in most states than in the general health care system. There are probably at least three consequences of the reduced reliance on cost containment approaches directed towards providers in workers' compensation compared to the rest of the health care system. First, providers who have had their fees squeezed by PPOs or Medicare fee schedules have not faced similar constraints in workers' compensation, and thus disparities in prices of similar services -- such as those in Minnesota -- exist between workers' compensation and elsewhere. Second, the limited use of utilization review in workers' compensation has allowed providers to provide more services, especially -- as also found in Minnesota -- for those conditions, such as back disorders, for which treatment protocols are less clear. Third, as cost containment has become increasingly stringent in the general health care system, providers have had increasing incentives to classify marginal conditions as work-related rather than nonwork-related, since the former category is more remunerative.

Workers as patients. Many workers have experienced a deterioration in recent years in the extent of protection they have

for nonwork-related injuries and diseases. Some employers have completely dropped health care benefits, and even when group health care plans have been continued, total benefits have in some instances been reduced. Moreover, many workers have been required to pay larger deductibles and coinsurance payments when they become patients.

Workers' compensation health care has retained certain essential attributes in most states in recent decades: there are no limits on the amount of health care; with rare exceptions, workers pay none of the workers' compensation premium for health care; and (again with rare exceptions) workers have no deductibles or coinsurance payments for work-related injuries and diseases.

The result of the deteriorating value of health care for nonwork-related injuries in contrast to the maintenance of the value of workers' compensation health care benefits is that workers' compensation has become increasingly attractive to workers when they are injured. For those conditions that are caused by a mixture of work-related and nonwork-related factors -- notable back disorders -- workers increasingly have an incentive to have these conditions classified as work-related.

The delivery system for workers' compensation. Many of the medical benefits in workers' compensation are provided not to cure the worker but to produce information that is needed to decide legal issues concerning the eligibility for benefits and the amount of the cash benefits. Thus, the worker and the employer (or carrier) obtain medical opinions about whether the injury or

disease was work-related; whether the medical condition has improved enough to allow the worker to return to work; whether the worker has reached the date of maximum medical improvement; and whether and to what extent the worker has a permanent impairment. Resolution of these issues makes the workers' compensation system inherently an intensive user of the health care system, and in at least some states, there appears to be increasing litigation in the workers' compensation program, which has probably led to an increase in these medical expenses.

Overtreatment promoted by insurance carriers. A recent book by Dr. Nordin Hadler has argued that for certain types of medical conditions -- notably back disorders -- there is excessive and unwarranted medical treatment. Hadler also argues that the primary responsibility for this overtreatment is workers' compensation insurance carriers, who require workers to undertake operations and other forms of treatment that are expensive and counterproductive.

Solutions Inside Workers' Compensation

There are several possible solutions to the rapidly increasing health care costs in workers' compensation. These solutions can be differentiated into those that can take place inside the workers' compensation program and those that involve reforms of the general health care system, including the health care component of workers' compensation.

Traditional Solution One: Fee Schedules. Fee schedules set maximum dollar limits on the amounts that health care providers can be reimbursed for their services. As of 1992, there were 27 states

with some form medical fee schedule.

Despite their widespread use in workers' compensation, there is only limited evidence of the effectiveness of fee schedules on limited health care costs. The most recent study by Pozzebon concluded that "the effect of fee schedules on moderating the rate of increase in medical prices is modest at best."

Traditional Approach Two: Limits on the Choice of Physician.

The second "traditional" approach to containing medical costs in workers' compensation has been to limit the employee's choice of physician and to allow the carrier or employer to control or influence that choice. Again there are only a few studies of the effectiveness of this approach to cost containment. The recent Pozzebon study found that limits on the employee's choice of physician were associated with increased medical costs, contrary to the expectations of those who promote such limits. This evidence is consistent with the argument by Dr. Hadler that carriers are likely to promote unnecessary and counterproductive treatments for certain medical conditions, notably back disorders.

New approaches for workers' compensation. The workers' compensation programs in several states are starting to introduce some of the cost containment approaches that have been widely used in the general health care system, including utilization review, HMOs, and PPOs. An example is the pilot projects authorized by 1990 Florida legislation. Preliminary results indicate that an HMO used for 17,000 state employees reduced workers' compensation medical costs by 38.5 percent. A second Florida pilot involving

7,500 private sector employees who received their workers' compensation medical care through a PPO network indicated that the managed care program saved approximately 3 to 4 percent of medical expenses.

Evaluation of inside solutions. The efforts to control health care costs within the workers' compensation program have not been generally successful to date, as demonstrated by the disparate growth rate of medical expenditures in workers' compensation compared to the general health care system, the considerable higher charges for similar injuries in the Minnesota workers' compensation program than in the state's Blue Cross program, and the few research studies of the traditions cost containment devices in workers' compensation (fee schedules and limits on employee choice of physicians), which provide little support for the effectiveness of these approaches. Perhaps the new approaches to cost containment in workers' compensation will be successful, although the preliminary evidence from Florida suggests a mixed record of success. The magnitude of the health care cost problem in workers' compensation and the concern that solutions internal to the program may be inadequate has led some to consider reforms that involve both the workers' compensation program and other components of the health care system.

Solutions Involving the Entire Health Care System

Some of the solutions to the high and rapidly increasing cost of health care in the workers' compensation program involve reforms of the general health care system, including the health care

component of workers' compensation.

Twenty-four hour coverage. Twenty-four-hour coverage plans eliminate the work-related test for cash benefits or medical benefits or both. One variant of twenty-four-hour coverage would integrate the medical component of workers' compensation insurance with health insurance for nonwork-related injuries. The resulting plan would provide medical benefits to workers around the clock, regardless of the origin of the workers' impairments.

Several states have authorized pilot studies of twenty-four hour coverage, and the idea has been discussed in a number of jurisdictions. The Clinton Administration has now recommended that workers' compensation health benefits be included as part of the health reform package, although actually this is not "true" twenty-four hour coverage since some distinctions between the benefits for work-related and other injuries would be retained.

The Clinton Administration proposal. The proposal has a number of features, several of which deserve mention: (1) The health plans selected by the employee would be responsible for providing treatment for work-related and nonwork-related injuries. (2) The employer (or carrier) would continue to be responsible for the costs of cash benefits and medical treatment for work-related injuries based on responsibilities under current law. (3) The employer would reimburse the health plan for the services provided for work-related injuries on a fee-for-service basis. (4) Each health plan must designate a workers' compensation case manager to coordinate the medical treatment and rehabilitation of the injured

worker. (5) The employer could purchase insurance that would require the insurer to pay for the cash and medical benefits provided for work-related injuries. (6) Workers cannot be required to share in the costs of the medical care through the use of co-payments and deductibles. (7) State laws limiting the employees' choice of provider for workers' compensation cases are overridden for workers who obtain medical care through health alliances.

A preliminary assessment of the Clinton Administration proposal. First, to invoke a cliché commonly pronounced by policy analysts, "If it ain't broke, don't fix it." I have devoted much of my testimony, however, to demonstrating that the health care component of workers' compensation is broke, and so a fix would be nice.

Second, what would work as a fix is not obvious. I have also spent a good deal of my testimony arguing that the traditional fixes for health care cost problems in workers' compensation -- namely fee schedules and limits on the employee's choice of medical provider -- appear to be of limited value and arguable only aggravate the medical cost problem they are supposed to help.

Third, one virtue of the Clinton Administration plan is the preservation of a financing mechanism for work-related benefits that continues experience rating. Most economists who have studied experience rating (whereby an employer's premiums vary with the record of workers' compensation benefits paid to that employer's injured workers) have concluded that experience rating matters in promoting safety. Indeed, a plausible case can be made that

workers' compensation experience rating has made a much more significant contribution to the promotion of workplace safety than has the OSHA program.

Fourth, the plan prohibits the use of deductibles and coinsurance for the medical care provided for work-related injuries. This prohibition eliminates one of the cost-containment devices that has been shown to be relatively successful in the health care system outside of workers' compensation. The argument is often made that requiring workers to pay for part of their health care would violate a fundamental principle of workers' compensation. I am not persuaded by this argument, in part because the cash benefits in workers' compensation rely on deductibles (the waiting period) and coinsurance (the replacement of only two-thirds of lost wages in most state laws). (I would not support the use of deductibles and coinsurance for medical care for work-related injuries unless something of value was given to workers in exchange.)

Fifth, the method used to determine the charges for medical care provided by the health plans that are reimbursed by the employer (or carrier) concerns me. The health plans receive fixed premiums based on risk characteristics of their patients so far as nonwork-related injuries are concerned. Coupled with this capitation payment system is a fee-for-service arrangement for work-related injuries, with the reimbursements of the health plan by the employer based on a fee schedule. This arrangement seems to invite cost shifting by health plans by classifying marginal cases

as work-related, by providing extra services for workers' compensation cases, and by using unbundling and other strategies to avoid the fee schedule.

The Clinton Administration plan does allow Alliances to negotiate per case capitation payments for workers' compensation cases, and one issue that needs to be explored during the deliberations on the proposal is whether capitation payments for workers' compensation can be made the basic method for reimbursing health plans rather than a possible alternative.

Sixth, a perplexing aspect of the Clinton proposal concerns the ability of employers or carriers to influence the amount and type of health care provided for work-related injuries. The provision of medical benefits is intertwined with the provision of cash benefits, and one danger of any plan that focuses primarily on reducing health care costs is that any savings there may result in higher cash benefits. For example, skimping on treatment may save medical expenses but prolong the healing period, thereby adding to the duration and amount of workers' compensation cash benefits.

The concern about the loss of control over the health care component of a workers' compensation case (because of the fear of the consequences for the amount of cash benefits) has led to resistance by some carriers (and employers) to the notion of relying on health plans as the primary source of medical care for work-related injuries. These carriers would prefer to keep workers' compensation medical care out of the health plans normally used by workers and in a separate set of health care providers

selected by the carriers.

I suspect that these carriers are making a serious mistake. As I indicated earlier in my testimony, the evidence from the current workers' compensation system suggests that those states that allow carriers to choose the treating physicians have higher medical costs, and the strong possibility exists that giving carriers the choice of treating physicians in all jurisdictions would covert a failed policy in selective states into a national failure.

Moreover, there are possible virtues of requiring employees to use the same health plans for work-related injuries as for nonwork-related injuries. Currently, in many states there are networks of doctors who specialize in workers' compensation cases, and some of these doctors overtreat and exaggerate the periods of disability and extent of permanent impairment. The Clinton Administration proposal would limit the ability of employees to doctor shop as part of the medico-legal process. I would urge carriers to carefully consider whether they would not be better off surrendering the ability to choose the treating physician (which is of dubious value anyhow) for the advantages of the health plan in which doctor shopping by employees is limited.

Chairman LaFalce, I hope this testimony is of value to the Committee on Small Business. I will subsequently submit a revised version of this testimony with references to the studies on which I have relied. I welcome your questions today.

John F. Burton, Jr.

Current positions: Director, Institute of Management and Labor Relations, Rutgers University since January 1991, and Acting Dean, School of Business - New Brunswick, Rutgers University since July 1993. Former positions include Professor, New York State School of Industrial and Labor Relations, Cornell University 1978-1990; Professor (initially Associate Professor) of Industrial Relations and Public Policy, Graduate School of Business, University of Chicago, 1966-1978; and Chairman, National Commission on State Workmen's Compensation Laws, 1971-72.

Publications include: with Steven L. Willborn and Stewart J. Schwab, Employment Law: Cases and Materials (Michie Company, 1993); with Terry Thomason, "Economic Effects of Workers' Compensation in the United States: Private Insurance and the Administration of Compensation Claims," Journal of Labor Economics, January 1993; with Alan B. Krueger, "The Employers' Costs of Workers' Compensation: Magnitudes, Determinants, and Public Policy," Review of Economics and Statistics, May 1990; Editor, New Perspectives in Workers' Compensation (ILR Press, Cornell University, 1988); with Terry Thomason, "The Extent of Collective Bargaining in the Public Sector," in Benjamin Aaron et al., editors, Public-Sector Bargaining (Bureau of National Affairs and IRRA, 1988); with Monroe Berkowitz, Permanent Disability Benefits in Workers' Compensation (Upjohn Institute, 1987); "Disability Benefits for Back Disorders in Workers' Compensation," in Nordin M. Hadler and Dennis B. Gillings, eds., Arthritis in Society: The Impact of Musculoskeletal Diseases (Butterworths, 1985); with Lloyd W. Larson, "Special Funds in Workers' Compensation," in John D. Worrall and David Appel, eds., Workers Compensation Benefits: Adequacy, Equity, and Efficiency (ILR Press, Cornell University, 1985); and with Charles Krider, "The Role and Consequences of Strikes by Public Employees," Yale Law Journal, January 1970.

Professional activities include Editor-in-Chief, Industrial Relations Research Association; Editor, Workers' Compensation Monitor, a bimonthly newsletter; Founding Member, National Academy of Social Insurance; and member of the Ohio Bar.

Research Interests include workers' compensation, social insurance, employment law, and public sector bargaining.

Education: B.S. Cornell (1957); LL.B. University of Michigan (1960); Ph.D. in Economics, University of Michigan (1965).

July 1993



STATEMENT ON WORKERS' COMPENSATION

before the

HOUSE COMMITTEE ON SMALL BUSINESS

for the

NATIONAL ASSOCIATION OF MANUFACTURERS

by

Charles D. Lein

September 29, 1993

**MANUFACTURING
MAKES AMERICA STRONG**



Manufacturing: The Key to Economic Growth

- ✓ U.S. manufacturing's direct share of the Gross Domestic Product (GDP) has averaged more than 21 percent since World War II. And nearly half of economic activity depends indirectly on manufacturing.
- ✓ U.S. manufacturing productivity growth averaged 3 percent during the 1980s compared with almost zero growth in the rest of the U.S. economy.
- ✓ U.S. manufacturing exports have been the *single main source of strength* in the current economy — contributing 30 percent to 40 percent of the nation's economic growth since 1987.
- ✓ Each \$1 billion of exports creates 20,000 new jobs. Since 1985, exports have saved 4 million jobs in U.S. communities.
- ✓ Manufacturing jobs on average pay 15 percent more than jobs elsewhere in the economy.
- ✓ Manufacturing provides the bulk of technological advances and innovation for the economy.

EXECUTIVE SUMMARY

The National Association of Manufacturers (NAM) and its member companies are committed to assuring that employees with injuries and illnesses which arise out of employment receive appropriate medical care (at no cost to the employee) and wage-loss benefits, if necessary. The current state run system, although jeopardized by rapidly rising costs, still serves the majority of claimants well. It is a minority of cases that has driven up the costs for everyone.

The cost of the current workers' compensation system for all businesses has nearly tripled since 1981. Although it is difficult to quantify this data for small business, due to the lack of complete and objective data, small businesses appear to pay to 5 - 10% more in higher premiums than those companies with comparable risks in larger corporations.

The Administration recently released a draft proposal that would include the medical portion of workers' compensation in it's overall health care reform proposal. An initial review of the proposal has generated many complex and unanswered questions. Primary concerns center on cost, case management, quality of care provided, litigation and dispute resolution.

The NAM will judge the Administration's proposal against a set of guidelines (See attached) and in the context of the overall health care reform bill. It should be noted that the NAM opposes federal involvement of the state run workers' compensation system.

STATEMENT ON WORKERS' COMPENSATION
before the
HOUSE COMMITTEE ON SMALL BUSINESS
for the
NATIONAL ASSOCIATION OF MANUFACTURERS
by
Charles D. Lein
September 29, 1993

Good morning, Mr. Chairman and members of the Committee. I am Charles D. Lein and with me today is Mark Stuart, associate director of risk management for the National Association of Manufacturers.

I am the president of Landstrom's Original Black Hills Gold Creations, a jewelry manufacturing company in Rapid City, South Dakota. I appear today on behalf of the Board of Directors of the NAM's Small Manufacturers Forum.

The National Association of Manufacturers is a voluntary business association of more than 12,000 member companies and subsidiaries, large and small, located in every state. Members range in size from the very large to the more than 8,000 smaller manufacturing firms, each with fewer than 500 employees. NAM members employ 85 percent of all workers in manufacturing and produce more than 80 percent of the nation's manufactured

goods. The NAM is affiliated with an additional 158,000 businesses through its Associations Council and the National Industrial Council.

Mr. Chairman, I'd like to thank you and the Committee today for the opportunity both to discuss the burden of escalating workers' compensation costs on small business and to discuss the potential benefits and weaknesses of the Administration's proposal to integrate the medical component of workers' compensation into a national health care plan. It is an issue that perennially dominates NAM surveys of both small and large manufacturers.

Traditionally, the NAM has long opposed federal involvement, in any way, of the state-run workers' compensation system. This remains current NAM policy. We have been, however, willing to discuss ideas that improve the workers' compensation system within the context of a national health care plan. We are currently evaluating the Administration's entire health care proposal and our position on workers' compensation will depend heavily on our position on health care reform. I would also like to say that the current system, although jeopardized by rapidly rising costs, still serves the majority of claimants well. It is a minority of cases that has driven costs up for everyone.

Before I review the burdens the workers' compensation has on small business and the pros and cons of the Clinton proposal, I would like to tell you about some of the problems our company faces with the existing system, even in a rural state like South Dakota.

Ours is a relatively small company by many standards, but is one of the larger jewelry manufacturers in the United States. We have 420 employees in Rapid City, South Dakota, and a network of independent representatives throughout the United States. We are currently celebrating our 75th anniversary.

A decade ago, our costs for worker's compensation were relatively insignificant. We have one of the safest, cleanest, most environmentally-correct work environments in our industry--worldwide. Yet, today we pay more in workers' compensation insurance each month than we paid per year only a few years ago.

While the vast majority of American workers do not abuse the system, an increasing number has become vulnerable to an abusive, expensive, free ride. For example, in California, and in other states, we have law firm "cappers" hanging out around unemployment offices, counseling claimants as to how "...their possible 'headaches' could be stress-related, having been brought on by conditions surrounding their employment." Nationwide, we have consortiums of attorneys and physicians advertising on TV, asking what musicians, grocery store checkers and factory workers share in common. They proceed to describe cumulative trauma/repetitive motion/carpal tunnel injury and advertise "no cost initial consultation."

Physicians are scared to death of malpractice lawsuits; insurance carriers are not overtly motivated to contain costs--they simply pass through escalating costs to the insured;

and an increasing number of attorneys are out "trolling for dollars!"

Not long ago, I became quite concerned when I discovered we had 11 of 13 active work comp cases in one department, on one shift. Almost all were relatively new employees, who had all been "stricken" with carpal tunnel. My curiosity was further peaked when I learned that a new employee was overheard asking what carpal tunnel felt like and "how do you get it?" Within 30 minutes, he also was stricken! About the same time, a lady in her late 20's was declared to be totally disabled, after having been trained as a solderer for only two months.

In another case, a new employee pulled an unauthorized radio in an unauthorized location off a shelf while stooping over. The radio hit him in the head and he has not worked since that accident. The case has cost us thousands of dollars, and there is no end in sight, as the employee goes from one specialist to another.

We were so concerned with what was happening that an office employee, who had no injury, asked if she could "test the system." The examining physician's opening question was centered around how much time she wanted off. By the time she was "thoroughly examined," she had a medication prescription, braces for both wrists, and was advised that she was a whisper from surgery on both wrists! I have asked physician friends how this could be. The response has consistently been that if someone says they "hurt," Physicians hardly dare challenge that response!

Small businesses fuel the engine of American enterprise. Almost every successful American business today was once small and struggling. My 27-year-old son, Keith, is a young retail entrepreneur. I recently asked him, "how did the numbers look last year?" He said he was working 80 to 100 hours a week, paid the mall \$65,000 rent, paid the bank \$45,000 on his loan, had a work force that seasonally ranged from 5 to 35, ...and paid himself \$4,200 for the year! My fear is that additional federal involvement in the workers' compensation system may cost small business more money than it saves, thus making it difficult for people like my son to be a future job provider.

Workers' Compensation Data

Accurate data on the change in the total cost of workers' compensation data nationally and state-by-state is difficult to obtain and almost non-existent for small business as a group.

With few exceptions, all employers are required to purchase workers' compensation insurance to ensure that workers who have become disabled as a result of an on-the-job injury or illness will receive compensation to pay their medical costs and to provide indemnity benefits for lost earnings. In all but four states, large employers are allowed to self-insure their workers' compensation risks and about 20 states allow, subject to many stringent requirements, groups of employers to pool their risks under group self-insurance plans.

Most small employers are not allowed to insure through these groups. As a result, most small employers have no choice, in most cases, but to pay the premium cost quoted by the insurance carrier.

By contrast, many large employers are able to have more than one carrier bidding for their business. We believe this results in premium costs that are 5-10% lower than for a smaller employer with comparable risks.

In recent years, the escalating costs of workers' compensation insurance for small employers has driven some out of business and caused others to curtail the hiring of additional employees - even though many of them have had no workers' compensation claims filed against them.

As noted, we cannot separate the trend in the cost of workers' compensation for small employers (as compared to large employers) with the limited information available. We can, however, look at total costs for all businesses and try to project some trends.

For many years the Social Security Administration has published data on the total cost of medical and indemnity benefits nationally and state-by-state. According to their reports the costs of cash indemnity and medical benefits have almost tripled during the ten year period between 1982 to 1992, from \$13.8 billion in 1981 to \$39.2 billion in 1991. I should note that this number represents "total payments" - not "total costs". For example, the

Social Security Administration estimates that total costs for private carriers and for state funds were \$43.1 billion in 1990 and \$7.9 billion for self-insurance in 1988.

Based on the information published by the Social Security Administration, The National Foundation for Unemployment Compensation and Workers' Compensation estimates the average costs of medical and indemnity benefits per covered employee have increased from \$186.00 in 1982 to \$438.00 in 1991 - almost tripling the cost. According to this Foundation, the growth rates have not slowed much in recent years. The per employee cost grew 11% - from \$348.00 to \$387.00 between 1989 and 1990 and by another \$13% to \$438.00 between 1990 and 1991.

Comments on the Current Workers' Compensation System

The NAM is concerned about the rising costs of health care (97 percent of our members provide it as part of their basic benefit package), as well as the increasing number of uninsured Americans. The high costs of health insurance make it increasingly difficult for Americans to compete globally.

We are also very concerned about sharp increases in the costs of workers' compensation which threatens the viability of many employers. Medical costs are rising faster in these programs than in general health care. Of the approximately \$70 billion spent last year on workers' compensation premiums, 60 percent of the costs were spent to

reimburse injured workers for lost wages and impairment. The remaining 40 percent covered medical costs, which were exacerbated by the fact that workers' compensation medical coverage is virtually unlimited in dollar amount and duration; without deductibles or co-payments; and subject to cost-shifting by providers to the workers' compensation system.

More than providing indemnity payments and medical care, workers' compensation is primarily a rehabilitation program. The goal of workers' compensation is to promptly restore an injured employee to his or her health and productivity. Prompt, high quality medical treatment for injured workers must be provided with this critical goal in mind. The most successful programs feature the ongoing involvement of the employer to ensure that the employee is fully supported in his or her total medical care and return to employment. Employer involvement ensures that, when possible, jobs are modified to foster rehabilitation and an early return to work.

Workers' compensation is also unique in that it provides all medical care at no cost to the employee. Full medical care is provided for the duration of the work-related injury or illness, regardless of where he or she may be employed. It can include physical therapy, chiropractic care, vocational rehabilitation and other services beyond the scope of many health plans. As government-funded plans such as Medicare and group health plans intensified cost-containment efforts over the past decade (which have limited reimbursement levels and services available), there has been a dramatic cost-shift to workers' compensation.

In addition to receiving payment for lost wages (indemnity benefits), employees know they can receive more treatment -- often by physicians of their choice at no cost -- through the current workers' compensation system. As a result, medical providers, facing stringent fee schedules and discounts in Medicare and group health care plans, often treat workers' compensation claimants with greater frequency and at significantly higher rates.

Both the emphasis on return to employment and the provision of comprehensive medical care at no cost to the employee, which are long-standing features of our nation's workers' compensation system, need to be understood in any proposal to include workers' compensation medical services in a national health care-reform package. While the costs of workers' compensation medical services are an increasingly important expense component, the majority of the workers' compensation expense is *still* devoted to providing benefits related to time lost from work (which also needs to be effectively controlled). As a consequence, an employers' current ability to influence medical treatment decisions thereby, facilitating rehabilitation and an employee's speedy return to work, must not be compromised in any new proposal.

NAM members applaud reform efforts at both the state and federal level. They will evaluate any proposal by the Administration dependent on its content as well as in the context of the health care reform proposal. Programs that contain costs, both in group health care and workers' compensation health care, would represent a substantial improvement over the current system. But workers' compensation has unique features that cannot be ignored if any

reforms are to succeed.

The Administration's Proposal To Integrate the Medical Component of Workers' Compensation into a National Health Care Plan.

In order to comment on the possible benefits and pitfalls of the Administration's proposal to integrate the medical component of workers' compensation into a national health-care plan, I would like to review how we understand the Administration's proposal on workers' compensation would work. At the end of this analysis, we have listed some comments and questions about this proposal which must be adequately addressed by the Administration before it can be fully understood.

As is widely known, the White House has proposed to reform the nation's health-care system, which would include the medical treatment of workers' compensation. Under the Administration's proposal, an injured worker would seek treatment from a provider participating in the health plan in which he/she is enrolled. For companies that self-insure their workers' compensation programs, the health plan will be one of the three or more plans directly or indirectly selected by his/her employer under the overall regional/corporate alliance system.

Under this plan, the health plan provider would treat the worker whether the injury is work-related or not. If the injury is work-related, the health plan will bill the employer (if

self-insured) or the employer's insurance carrier (if coverage is purchased on the open market) for the care provided. The rate of reimbursement is to be at the alliance fee-for-service schedule unless another fee is negotiated with the health plan. To that extent, cost-shifting could be reduced, if the fee-for-service schedule is similar to the cost of providing similar services under general health care. This appears to be the goal of the program.

The issue of work-relatedness and extent of compensable injury are to be determined under state compensation law, which appears to mean thorough the workers' compensation adjudication process. In practice, in contested cases no reimbursement should be paid until the state adjudication process has made the compensability determination. Thus, reimbursement claims of health plans/alliances stand in the same shoes as claims of medical providers under existing workers' compensation laws. The only difference is that the amounts may be lower under the proposal because of previously negotiated rates that cut costs through negotiations, which may be lower than the prescribed fee schedule.

Employers would not be "relieved" of their current statutory obligation to pay separate insurance premiums (or to self-insure) to indemnify employees for lost wages.

Background on This Issue From the NAM's Perspective

The NAM's Workers' Compensation Subcommittee has developed a set of guidelines which it will use to judge the inclusion of workers' compensation in any national health care

proposal. (See attached.) My following comments on the pros and cons of integrating the medical portion of workers' compensation reflect an initial analysis by NAM's Workers' Compensation Task Force using these guidelines. Our review generated many more questions and comments than it did identifiable pros and cons, so I have listed those comments and questions after our preliminary analysis. As a result, our comments are preliminary and general in nature.

It should also be noted that states such as Florida, Oregon and Washington are experimenting with workers' compensation reform programs; and we would suggest it may be premature to implement reform at the federal level without giving the proper time to determine the effectiveness of these state reform plans.

Possible Benefits of Integrating the Medical Portion of Workers' Compensation in a National Health Care Plan

Fee Schedule

As mentioned above, it appears that the Administration's proposal may include the application of a fee schedule to workers' compensation injuries. The Administration's draft position on this issue indicated this possibility, but it is difficult to determine what the protocols for treatment will be under this plan. Protocols could make or break the effectiveness of the new system.

Negotiated Fees

A second possible benefit may be the possibility of negotiated fees with providers for workers' compensation injuries. Under the Administration's proposal, it appears that health care providers may be able to negotiate lower fees than the suggested fee schedule.

Providers

The proposal does contain a provision that could reduce or eliminate self-referrals. In the current system, self-referrals have aggravated workers' compensation costs.

*Potential Problems With the Integration of the Medical Portion of
Workers' Compensation in a National Health Care Plan*

Case Management

The ability of the employer to be involved early in the employees return to work, (i.e., working with the physician to clearly diagnose the problem; working with the health care provider to determine the appropriate treatment; and then modifying job duties when possible to get the employee back to work as soon as possible) is key to the success of an employee's return to work.

The Administration's proposal appears to reduce employer involvement and control over medical care by mandating that the health alliance play the dominating role as a case manager. This provision could build a barrier between the employer and the employee. A

health-alliance case manager is not in the best position to advise on the employee's recovery. This task requires an in-depth knowledge of the workplace, job requirements and capabilities of the employee. It is best accomplished by employer case managers.

This plan would also affect the ability of the employer to direct specific cases to true specialists for occupational injuries and rehabilitation. All doctors are not equal. Some are much better suited to handling these tasks and have experience in workers' compensation. In many cases, employers are familiar with the most effective health providers of work-related injuries and illnesses.

Employees generally do not have the knowledge, training or experience to select the appropriate specialist for treatment of work-related injuries. Most consumers have some experience and understanding of the procedures and treatment patterns for ordinary illnesses treated by family practitioners and, therefore, can make informed choices for their primary care physician. This is not the case with occupational injuries. For most people, this is a once-in-a-lifetime experience. They do not have any knowledge or experience on which to base their choice. Employers or carriers have the experience to make a decision and get the best medical care for their employees.

Cost Shifting

Under the current workers' compensation system, there are no co-pays or deductibles. The Administration's proposal would continue this practice. Many in the employer

community believe the lack of co-payments and deductibles for workplace injuries and illnesses and the chance to receive indemnity benefits have long been a source of shifting costs from group health to the workers' compensation system. The NAM does not endorse and is not suggesting that co-pays and deductibles be a part of a new system; but we point cost-shifting out as a problem that exists now and would continue to exist under the Administration's proposal.

We would also point out that, under the Administration's proposal, the provider seems to have no reason to dispute a workers' compensation claim. Treating an injury under the alliance plan would be new revenue to the health plan, as opposed to treating an injury under regular health insurance, which would be a loss to the provider and must be paid for out of premiums. Thus, there remains an incentive for the provider to treat an injury as a workers' compensation claim.

Litigation/Dispute Resolution

Under the Administration's proposal, there is a segregation of medical aspects from the state-controlled disability components, which will likely lead to disputes and litigation. Potential difference in plans from state to state may create an incentive for employees to switch jurisdictions for claims, which could lead to additional litigation.

A new national system will complicate administration of claims for employees working and living in different or multiple states. What happens when an employee is injured

on the job out of the state in which he/she lives? What if that employee, for example, a severely burned person, requires hundreds of thousands of dollars of emergency medical treatment? We are concerned that there will be a dispute between alliances, especially over more costly injuries. The result may well be new litigation between the alliances for such costly treatment.

*Comments About the Integration of the Medical Portion of
Workers' Compensation Into a National Health Care Plan*

Safety in the Workplace

The draft proposal makes no specific references for maintaining a safe workplace. We do understand that the Administration is trying to add language to its proposal that would reflect that any savings achieved by maintaining a safe workplace would be reflected in a company's workers' compensation premium. Self-insured companies would continue to have that incentive via lower medical and indemnity costs.

Experience Rating

Experience-rated premiums appear to be maintained in the Administration's proposal, but there is little detail on this feature.

Return to Work

This is the single most important issue in workers' compensation. Indeed, it is the

primary goal of the program. Success today is largely due to employer or carrier control and involvement. "Health alliance case managers," mentioned in the proposal, are not a good or valid replacement for carrier/employer case management. They will not necessarily know the employer, the workplace, job function or employee as well as employer case managers. This lack could seriously hinder return-to-work efforts. One way this could be addressed would be to allow case management by the employer or carrier. If the employer elects not to do this, then the health alliance case manager would assume control. The use of an employer case manager should allow for a negotiated fee reduction with the health alliance.

The success of the Administration's proposal is also dependent on the true credentials and abilities of the certified medical providers. There is no discussion in the proposal on what criteria or credentialing standards would be used to determine the qualifications of these providers or of the case managers.

Determination of Work Relatedness

The proposal is silent as to who has the authority or responsibility for this decision. It states that the disputes would be settled in accordance with existing state laws, but it does not state who will make the initial determination. If the health alliance has control and there is a differentiated fee structure for work-related and non-work related injuries, there will be major cost-shifting.

Costs

It is unclear what, if any, cost saving will occur under this proposal. It depends heavily on the unanswered questions listed here. If any changes in the system artificially increase the use of the workers' compensation system, it could have dramatic impact on indemnity costs, thus outweighing any savings on medical costs.

Treatment Standards

The proposal mentions the use of protocols, but it is unclear which one and how they will be developed. We understand some have been drafted.

Fraud

Fraud is addressed in another part of the health care proposal. We remain hopeful that fraud could be discouraged through civil and criminal remedies.

Commission on Health Benefit and Integration

A commission is called for in the Administration's draft proposal to "report to the President and present a detailed plan for integration, if it is recommended, on or before July 1, 1995." We are very concerned that this commission's report may be the first step in federalizing the entire workers' compensation system. We do not feel that this is in the best interests of the employer or employee.

Group Self-Insuring for Small Employers

Because of the high cost of workers' compensation for small employers, many have turned to joining with other companies to group self-insure. This has become a popular and effective alternative to purchasing insurance on the market. We would like to see provisions made for the continuation of these "clubs" under any new proposal.

Questions About The Integration of Workers' Compensation in the Health Care Proposal

1. The fee structure is ambiguous. Can medical providers have a different fee structure for work-related and non-work related injury treatment?
2. Who will certify medical providers to treat worker injuries? What will be the certification standards?
3. Do employers/carriers continue to have the ability to make the initial determination of compensability? Who pays for the treatment on denied claims? The alliance?
4. Can the employer/carrier medical case managers oversee treatment on compensable injuries if the worker is treated under a health alliance?
5. What happens if a case manager disagrees with the diagnosis, treatment plan or extent of disability determination of a certified provider?

6. Who will determine "appropriate protocols" for treatment of workers' compensation injuries?
7. For referrals to specialists outside the alliance, what fee schedule applies?
8. Will the ability to negotiate rates below the established schedule allow the health providers to shift costs to smaller customers?
9. What are the performance measures/standards for assessing providers? What are the penalties for poor performance?

Conclusion

As you can see, this is a very difficult and complex issue to address. We do acknowledge that if the health care system is going to be changed, the workers' compensation portion must be addressed as well. If not, the workers' compensation system will be doomed to cost-shifting.

We will review any health care reform proposal that includes workers' compensation against our guidelines and in the overall context of the health care reform proposal. This review will be provided to the Committee when it is available.

We will also develop a position on what the manufacturing community would like to see done with the system.

It is important to understand that no reform proposal has ever been so seriously considered at the federal level. We must urge great caution be given to such a discussion. The current system, for all its problems, does serve the majority of claimants well. It is a minority of cases in combination with systemic problems that have complicated the system.

The NAM along with the AFL-CIO, co-chair The Labor-Management Discussion Group on Workers' Compensation. We have been meeting for more than two years on a regular basis. Our primary focus has been on issues related to the two most important players in the system; the employee and the employer. We have developed white papers which our peers can use at the state level as a guide to solving some of their problems. We will try, over the next few months, to do the same on this issue.

NAM members are concerned about their employees. They want to continue to provide them with affordable, high quality health care. Many of the programs voluntarily provided by NAM companies provide the best protection available today at very competitive prices. We hope that the programs developed by the Administration will allow us to continue to provide affordable, quality care for our employees.

Although some proposals currently under discussion are not necessarily what the NAM would suggest, we remain willing to explore the concept and trust that our words will carry weight in the legislative process. It should be noted that most of our business and industry associations are opposed to any federal involvement with state workers' compensation programs.

Mr. Chairman, thank you for the opportunity to address the Committee on this critical issue. I would be happy to answer any questions that you may have.

***GUIDELINES BY WHICH THE NAM WOULD JUDGE ANY PROPOSAL THAT
WOULD INCLUDE THE MEDICAL PORTION OF WORKERS' COMPENSATION IN
THE HEALTH CARE REFORM PROPOSAL***

Safety in the Workplace

Good safety practices protect employees. Injury prevention should be a primary focus of employers. Employees must recognize their personal responsibility to ensure their own safety.

Self-Insurance

Self-insurance promotes employer accountability. Since the employer is directly responsible for medical and indemnity losses when it self-insures, self-insurance should remain a viable alternative for financially responsible companies. Case management must stay with employers, as only employers have real incentives to minimize costs.

Experience Rating

Pricing should remain "risk-adjusted" to ensure that prior safety and wellness efforts by employers and employees are reflected and encouraged to continue.

Return to Work

The focus of any workers' compensation medical system must be to achieve the timely return to work of any injured employee.

Determination of Work-Relatedness

Under any proposal to include the medical portion of workers' compensation in the health care reform bill, care must be taken to ensure that a physician's opinion on causation and the extent or duration of impairment not be influenced in any systematic way. For example, in a merged system, the physician in an HMO may have an incentive to characterize the injury as work-related if the HMO is entitled to a premium adjustment for its volume of workers' compensation cases. In addition, whatever this effect would have on medical costs, it will certainly have an effect on indemnity costs.

All Inclusive

If the medical portion of workers' compensation is included in the national health care reform proposal, all workers' compensation *medical* programs under both state and federal laws should be included. Individual jurisdictions should not have the option to opt out of the system.

Costs

Any federal system mandating or affecting employer-provided health insurance programs must also be mindful of the unique character of workers' compensation-related medical benefits and take all necessary steps to prevent cost shifting from the former to the latter.

Any statutory changes implementing a system combining elements of health insurance and workers' compensation-related medical services must lead to overall financial savings for employers that presently provide both.

Overall system costs must be decreased, including the indemnity costs associated with workers' compensation. Whether or not there is a role for cost sharing by employees will have to be further explored. The NAM recognizes the controversial nature of this issue, but also realizes that a new health system may contain proposals not traditionally considered.

Simplification should reduce unnecessary, non-productive costs and services. Elimination of these costs will make more dollars available for care.

Treatment Standards

There must be treatment standards that prescribe the protocols to be used and the duration of treatment. Services for work-related and non-work-related injuries should be uniform. There should be no perverse incentives for providers to select workers' compensation versus group health. It is understood that certain additional services for work-related injuries may be needed over and above the basic treatment standards, such as physical therapy and vocational rehabilitation.

Providers

The quality of care available should be retained or improved, but inappropriate

medical treatment, testing and delays in returning injured employees to work must be prevented.

Medical providers should maintain objectivity and independence in fact and in appearance. The program should discourage all self-referral by medical providers.

Comprehensive, specialized services must be readily available to treat work-related injuries.

Employers

Employers must retain the ability to manage work-related medical and disability benefits. Employers should work closely with medical providers in the design of meaningful rehabilitation programs. Employers should exercise the sole choice over workers' compensation provider/services.

Litigation/Dispute Resolution

Any proposal to include the medical portion of workers' compensation in a national health care system should be designed to reduce medical/legal issues. State or federal workers' compensation agencies should retain the authority to settle disputes.

The "exclusive-remedy" provisions of workers' compensation should be preserved and even enhanced to reduce non-productive costs of litigation.

All present employer defenses and procedural due-process rights under federal and state compensation statutes must be preserved. No presumption, inference or estoppel theory can attach to any medical treatment provided under the proposed system, i.e., the HIPC (or whatever it is currently called) must have no role whatsoever in determining causality.

If there are provisions in any health care reform proposal aimed at preventing criminal and civil fraud and reducing excesses in medical malpractice litigation, these same provisions should be available to workers' compensation medical litigation.

Fraud

Fraud by any party should be subject to criminal and civil penalties.

Health Care Administering Agencies (Health Alliances/HIPCs/AHPs, etc.)

No health insurance reform proposals should carry requirements to collect and forward to federal government agencies (such as OSHA) information on occupational injuries and illnesses. Current reporting requirements should remain with the employer.

Indemnity

The new system cannot be a vehicle to expand any federal mandates or benefit expansion of workers' compensation indemnity benefits.

Employer-Provided Emergency Medical Services

Employers must be able to continue to provide on-site emergency medical services under any health care proposals.



1155 15TH STREET, N.W.
SUITE 710
WASHINGTON, D.C. 20005
202-293-8830
FAX: 202-872-8543

Statement of

**Polly Reber
Director of Government Relations
Small Business Association of Michigan**

**Before the
House Small Business Committee**

**Regarding
Health Care Reform**

**On Behalf of
National Small Business United and
Small Business Association of Michigan, member**

September 29, 1993



222 N. Washington, Suite 310, P.O. Box 16158, Lansing, Michigan 48901-6158. Phone 800-362-5461

Testimony of Polly T. Reber
before the U.S. House Committee on Small Business
September 29, 1993

Mr. Chairman, members of the committee, I appreciate the opportunity to appear before you today. My name is Polly Reber, I am Director of Government Relations for the Small Business Association of Michigan. Our organization is a private, non-profit, multi-service trade association representing over 6,600 small businesses across the state of Michigan. While the criterion for membership is 250 employees or less, the overwhelming majority of our members have 25 or fewer employees, closely reflecting the population of the business community as a whole. The Small Business Association of Michigan is also an affiliate member of National Small Business United, in Washington, D.C.

The state of Michigan has a relatively good workers' compensation insurance system overall. The problem is we cannot afford it and the reason is spiraling health care costs. Work comp has long been cited by small businesses as one of the most burdensome costs of doing business in Michigan. In our first edition of Small Business Barometer, (April, 1993), a publication which not only measures performance but also tracks the expectations and experiences of Michigan's small

businesses, work comp costs was mentioned frequently by small business owners as the aspect of Michigan's business climate which was most negative. Because it is a function of payroll, it is a disincentive to job creation or expansion. Any decision to hire more employees must be weighed against the negative impact of work comp costs. This is a significant threat to small businesses which are currently the largest producers of jobs, not only in Michigan, but also the nation.

Small businesses do not enjoy some of the advantages the work comp system extends to larger companies. Besides the obvious advantage of having greater resources to absorb the financial shock of increasing rates, big businesses can form self-insured funds and can negotiate more favorable rates with insurers. While some small employers can and do join group self-insured funds, that option is not available to all small employers. A small business with a history of few or no worker injuries could end up in a risk pool for their industry and thus pay the increased rate along with companies with higher injury experience. Michigan's small businesses also find themselves at a competitive disadvantage with many other states, most especially Indiana, our neighbor to the south, which has much lower work comp costs. At a time when small businesses need to grow by expanding into markets in other states, Michigan's work comp make our businesses less competitive due to greater benefit costs.

Over the last decade, Michigan has made significant changes to our work comp system. In the early 1980's, Michigan changed from a state approved rate classification for businesses, to an

open rating system whereby every insurance company could file and set their own rates for businesses, introducing competition into the system. Today, Michigan has the second lowest number of businesses (12.9%), in the Placement Facility for assigned risk, which is the insurer of last resort.

In the late 1980's, Michigan began implementing comprehensive health care services rules and a fee schedule for work comp. The fee schedule sets a maximum fee a provider may charge for any work comp health care service. The rules established a utilization review process to be the responsibility of the carrier, they include a data collection requirement, and a dispute resolution process. It is estimated that the implementation of the rules has saved our work comp system 20% per year.

Michigan has achieved some degree of success in controlling the dramatic increases within the work comp system. As an example, Michigan is one of only two states (the other being Florida) which has implemented six common cost containment strategies in workers' compensation as identified by the Workers Compensation Research Institute: 1) limited initial provider choice; 2) limited provider change; 3) medical fee schedule; 4) hospital payment regulation; 5) utilization review; 6) bill review.

Along with rising legal costs, the expansion of job related injuries in recent years to include such things as stress, carpal tunnel syndrome, and age-related ailments has contributed to increased work comp costs. However, the most significant factor has been the spiraling cost of health care

in this country. The health care component of work comp accounts for approximately 40% of the total costs of work comp. Although Michigan's efforts to address costs have seen results, within the larger context of dramatic health care cost increases, our work comp system has become a real financial burden for small business.

As a means to addressing this problem nationally, there have been proposals to integrate the health care component of work comp into a national health care plan. Although this may initially seem like a logical step, there is good reason to be extremely cautious with this idea. First, national health care reform is a monumental task. The complexities and challenges of reform are almost overwhelming. To add the health care component of the workers' compensation insurance system to that task at this time could devastate the system. Once we begin moving toward reform in health care, there may be a need to bring in the health care components of other systems such as work comp. However, we need to proceed carefully to achieve success in creating an effective, quality health care system, first. If reform in health care is achieved, many of the concerns with the health care component of work comp will be addressed. At that point, it will be important to analyze integrating work comp into the system. Issues such as coordination of benefits and dual coverage are relevant to that discussion. Although work comp health care has increased overall more rapidly than health care in general, it amounts to only about 3% of total health care costs.

Secondly, the goal of the health care component of work comp is a little bit different than the goal of health care in general. When a worker is injured on the job, the work comp system is designed with a goal of getting the worker back to work as quickly as possible. Work comp must provide indemnity and vocational rehabilitation benefits as well. The health care component is factored into a system which also includes prevention, disability management, and return to work programs.

Workers' compensation insurance is of great value to small business. It creates responsible means by which employers assist and protect their employees should they be injured on the job. It also contributes to a safer and thereby more productive work environment. The Small Business Association of Michigan and National Small Business United supports reforms in the work comp system to achieve those ends without financially overburdening a most essential part of our economy, small business; just as it supports reforms in the health care system with similar qualifications. And while we deperately need relief from high work comp costs, the method to achieve that may not necessarily be within the parameters of national health care reform.



NFIB
National Federation of
Independent Business

STATEMENT OF

JON EGGE
M P PLUMBING
CLACKAMAS, OREGON

Subject: Workers' Compensation and Health Care Reform

Before: Committee on Small Business
U.S. House of Representatives

Date: September 29, 1993

Thank you for this opportunity to testify before the Committee on Small Business on the important subject of workers' compensation and how it may be integrated into the new health care reform plan. I appreciate the opportunity to testify and share my views and those of the National Federation of Independent Business (NFIB) whom I am representing today on this important subject.

NFIB is the nation's largest small business advocacy organization, representing more than 600,000 small and independent business owners nationwide.

Introduction

The latest NFIB survey on the **Problems and Priorities** of small business showed that workers' compensation ranked fourth out of 75 problems facing small business. If you exclude from the survey those employers who do not have any employees (and thus do not have to purchase comp for their employees), workers' comp becomes the number two problem. Only health insurance ranks ahead of workers' compensation in terms of its impact on NFIB members. Why this concern about comp? Two words--premium increases.

Workers' Compensation Premiums Are Rising

Workers' compensation premiums are based on the total payroll of the employer (x dollars per \$100 of payroll). There are two kinds of ratings in workers' compensation--manual rating and individual experience rating. Only those businesses that pay a certain level of premium are individually experience rated. While workers' compensation is not a "tax," it operates the same

as a payroll tax, since it is mandatory for almost all employers and it is based on each one hundred dollars of payroll.

Workers' compensation premiums in recent years have been rising at an alarming rate. The National Council on Compensation Insurance (NCCI), the major workers' comp rating organization, received approval for double-digit rate increases last year in 20 states. The NCCI rate increases exceeded 20 percent in six states (Florida, Kansas, Louisiana, Missouri, Nebraska and Oklahoma). The average premium rate increase nationwide in 1992 was 10 percent.

This premium rate activity follows eight years of rising average premium increases approved by state regulators (11.5 percent in 1985, 8.9 percent in 1986, 9.6 percent in 1987, 8.9 percent in 1988, 6.1 percent in 1989, 12.1 percent in 1990, and 7.4 percent in 1991. Keep in mind that these are the rate increase levels actually approved by state regulators. Insurance industry rate requests were much higher. For example, in the last five years insurance carriers have only gotten about half of the premium level increase requested (52 percent in 1988, 47 percent in 1989, 55 percent in 1990, 55 percent in 1991, and 64 percent in 1992).

Premiums Driven By Benefit Payouts

Why are workers' comp premiums rates soaring? The simple answer is benefit payout. During the period 1981-1990 workers' compensation medical and cash indemnity benefits increased from \$12.5 billion to \$35.3 billion, up 183.4 percent. The average benefit cost per covered employee rose by \$222, an increase of 134.3 percent. The benefit cost ratio (benefits as a percent of payroll) increased 55.1 percent.

In 1990 the average workers' compensation benefit cost per employee ranged from \$768 in Maine to \$177 in Indiana. The national average for the states was \$387. Joining Maine in the top ten states in terms of highest average benefit costs were West Virginia (\$712), Rhode Island (\$651), Texas (\$645), Alaska (\$623), Nevada (\$623), Montana (\$604), Louisiana (\$530), Massachusetts (\$525) and Oregon (\$515).

In addition to Indiana, lowest average benefit costs per employee were recorded in North Carolina (\$179), Virginia (\$197), Nebraska (\$208), Iowa (\$214), South Carolina (\$229), Vermont (\$250), South Dakota (\$255), Missouri (\$255), New York* (\$257) and Wisconsin (\$257).

Data from the National Council on Compensation Insurance based on detailed claim information for eight states (Florida, Georgia, Illinois, Kentucky, Massachusetts, Michigan, Minnesota, and Pennsylvania) show the average total cost per lost time claim rose from \$16,682 in 1988 to \$22,795 in 1991 (up 36.6 percent). The average indemnity cost per lost time claim increased 30.1 percent, rising from \$11,515 in 1988 to \$14,978 in 1992. The average medical cost per claim during this period went from \$5,167 to \$7,817, an increase of 51.3 percent.

Accompanying the rising costs of indemnity and medical payments was the unfortunate increase in the number of lost work days resulting from occupational injuries. During the period 1988-1992 the number of such injuries per 100 full-time private sector workers climbed steadily:

* New York increased benefits subsequent to this data collection period.

76.1 in 1988, 78.7 in 1989, 84.0 in 1990, and 86.5 in 1992. NFIB is concerned about the workplace safety issue and has supported the enactment of legislation providing for an optional employer-paid deductible as an incentive for employers to maintain a safe worksite. We have also supported legislation providing premium credits for a history of safety.

Benefit payout is the driving force behind premium levels. But what drives benefit payout? There are, in fact, a number of factors that drive benefit payout: (1) the cost of medical care; (2) the amount of litigation in the system; (3) the definition of compensable injuries and illnesses; (4) the duration of compensation; (5) the number of occupational injuries and illnesses; and (6) fraud and abuse in the system. We need to look at who gets into the system, how cost-effective is the treatment and care of these people, and how long they stay in the system.

Medical costs are rising dramatically--even faster in workers' comp than in the other areas of health care. For example, during the period 1980-85 general medical costs rose 10 percent annually, but workers' comp medical costs increased by 14.5 percent on an annual basis. One reason for this is that we have not yet introduced traditional medical cost-containment mechanisms into the comp system--primarily because comp medical benefits, and the delivery of these benefits, are defined in statutory law. There is a litany of medical cost containment measures that states should consider incorporating, such areas as medical fee schedules, utilization review, provider selection mechanisms, PPOs and HMOs. The point is that state comp programs must not become the last safe harbor from effective medical cost containment.

Another major problem in comp programs is increasing litigation. The passage of comp laws early in this century reflected a great compromise between labor and industry in which both sides agreed to take industrial accidents and illnesses out of the tort system and into a no-fault insurance system. Employees gave up the right to sue employers for negligence, and employers agreed to pay claims to injured workers regardless of fault or negligence. The injured employee, however, was allowed no other remedy outside workers' compensation. Employers, while benefiting from this exclusive remedy doctrine, agreed to relinquish their common law defenses and accept responsibility for employee compensation even if no employer negligence was involved in the injury.

That was the deal. Business accepted it. Labor accepted it. Sadly, someone forgot to tell the plaintiffs' lawyers. Thus, the litigation explosion.

A third area of concern to employers is the ever-expanding definition of what constitutes an occupational injury or illness. To what extent is mental stress or a cumulative injury job-related? The state legislatures and the courts continue to expand the definition of a compensable injury. The concept of cumulative injury is being pressed forward to expand the scope of comp coverage to include claims arising from maladies traditionally associated with the aging process.

It is becoming increasingly difficult to distinguish between a work-related and a nonwork-related disability, and the comp system is becoming a general health care policy. Couple this with the fact that there are economic incentives for employees to utilize comp rather than the health policy, and you have system on the verge of spinning out of control.

Finally, many employers have not been as responsible as they should have been in terms of getting injured employees back on the job as soon as they are able to return. One of the reasons lawyers get involved is because injured employees feel all alone since they have lost touch with the employer and the workplace. When they start feeling that way, they start looking for help. Employers should keep in touch with injured workers. They should call them and tell them they are missed. Employers should ask them when they can return and invite them to visit the workplace. Employees should be encouraged to return to work at whatever capacity they can handle. Better they should be at the workplace, at whatever level of productivity, than to be sitting home watching those lawyer ads on television.

The tremendous increases in workers' compensation costs have led to calls for reform of the system from almost all quarters. Indeed, some significant reforms have been adopted in a number of states. One of the reforms some are calling for, some kind of combination of workers' comp and health insurance, has not been implemented. At the state level this reform is referred to as 24-hour coverage and usually entails combining comp and health. At the federal level we refer to the "merged" or "integrated" approach (splitting off the medical portion of comp and merging it into a new national health plan) and the "coordinated" approach (simply allowing or requiring comp medical claimants to be treated by the Approved Health Plans).

The Administration is considering incorporating the medical portion of state workers' compensation programs into the proposed new national health care plan. This proposal could take one of two forms: (1) actually separating the medical aspect of workers' compensation from the disability (or wage loss) component and moving it into the new national health care plan; or

(2) simply maintaining the current workers' compensation medical and disability programs and allowing workers' compensation insurers to contract with the qualified health plans for the treatment of workers' compensation medical claims. Having looked at both the merged approach and the coordinated approach, the Administration has apparently decided to go with the coordinated approach as a first step, and appoint a Commission to study how they might move to a full merger. The Administration's Health Care Task Force concluded, and we believe rightly so, that there were a number of problems inherent in splitting the comp program and merging the medical portion into national health, and they wanted additional time to study how these problems might be resolved.

Many in the Administration seem to favor the idea of separating the medical portion of workers' compensation from the disability component. Under this kind of proposal, medical would become part of the new national health care structure and disability would remain under the purview of existing workers' compensation carriers. In anticipation of such a proposal, NFIB recently polled its members on this concept (**Mandate 501, June 1993**). The following question was posed: "Should the Medical Portion of Workers' Compensation be Moved Into a New Standard Health Plan?" Appropriate background information was provided to the membership, including pro and con arguments. The results were 19 percent voting in the affirmative, 63 percent voting in the negative, with 18 percent undecided.

Considering the fact that workers' compensation is mandatory for most employers and that the costs for this insurance are rising faster than general health insurance, one might think that employers would opt for any kind of change that offered some hope of reducing costs. Indeed,

the Administration has put forth its proposed merger of health insurance and workers' compensation medical as a cost containment measure. Clearly, NFIB members did not view it as such. Since workers' compensation medical expenditures are less than 2 percent of all health care expenditures, it is hard to conceive of the merger approach as a major cost containment mechanism. Some members of the Health Care Task Force have touted a recent study by Alan Krueger and Laurance Baker as evidence that a merger of health and comp would result in enormous cost savings. Rick Victor of the Workers' Compensation Research Institute has closely examined the Krueger-Baker data and is not convinced. Victor's critique of the Krueger-Baker study leads him to this conclusion:

"Even if it were true that there is price discrimination or procedure upgrading against workers' compensation, this would not be a strong argument for twenty-four hour coverage as a solution. Price discrimination arises because there is a difference in the attention the consumer (patient) pays to price. Workers' compensation patients, without cost sharing (deductibles and copayments) may well be less price sensitive than group health patients who share in the cost of their care. But twenty-four hour coverage would only change this if it imposed patient cost sharing; it is the cost sharing--not administrative integration--that could reduce any price discrimination. A national health plan without patient cost sharing for work-related injuries would not change this, and cost sharing could be introduced with or without national reforms and twenty-four hour coverage. Regardless of the form of administration, policy makers must decide whether equity for injured workers precludes patient cost sharing and other cost control methods. All this suggests that \$6 billion in savings will not simply fall out of an administrative integration of workers' compensation with group health benefits. There are no easy fixes to the workers' compensation medical cost problems. System participants will have to face tougher problems of finding ways to effectively control utilization while preserving access to high-quality care. And, this will be true whether workers' compensation is included in a national health reform plan or not."

Under either the merger approach or the coordinated approach, any cost savings are likely to occur as a result of getting workers' compensation medical claimants into a managed care

environment. This can be achieved without dismembering the current workers' compensation program.

There are, in fact, several technical problems in merging workers' compensation and health insurance. These revolve around the difference between health and comp in such areas as experience rating, scope of coverage, extent of coverage, benefit levels, cost sharing, and so forth. In addition, splitting the system into two parts means that employers/insurers might lose some control over the disability case management aspect of workers' comp. Eliminating the rehabilitation and return to work supervision of employees could seriously inhibit the ability to control costs on the disability side. Administration officials have come to recognize that these problems are significant and are beginning to give serious thought to how they might be resolved.

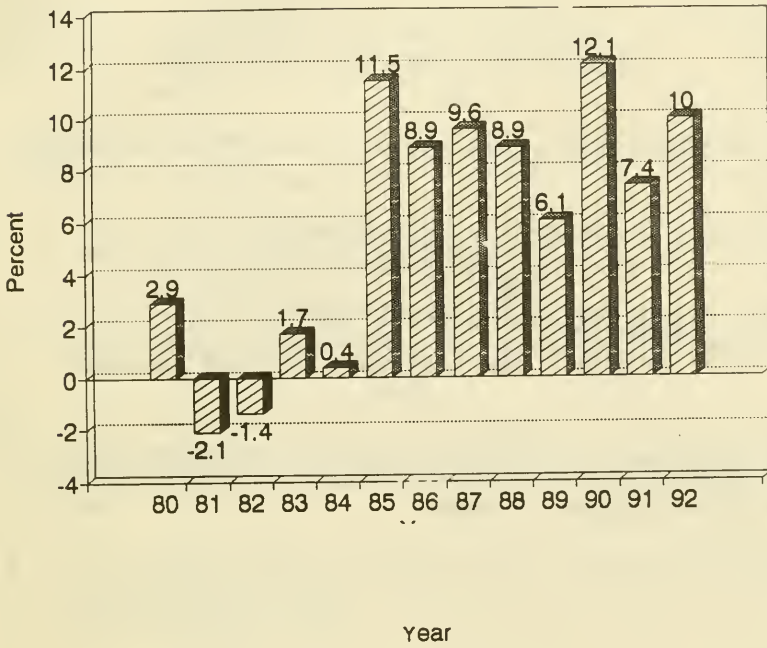
Since most employers are required to carry workers' compensation, they have some understanding of the program, and they understand that workers' compensation reform is absolutely essential. It will be difficult, however, to convince them that a merger of the health and comp systems represents the road to reform if the technical problems outlined above cannot be resolved.

NFIB appreciates efforts by the Administration and others to mitigate the workers' compensation burden on small business. We believe, however, that the case for a merger approach has not yet been effectively made. A "coordination" policy that allows cost-saving managed care programs to be applied to workers' comp cases would be far preferable and, we believe, more palatable to employers and insurers.

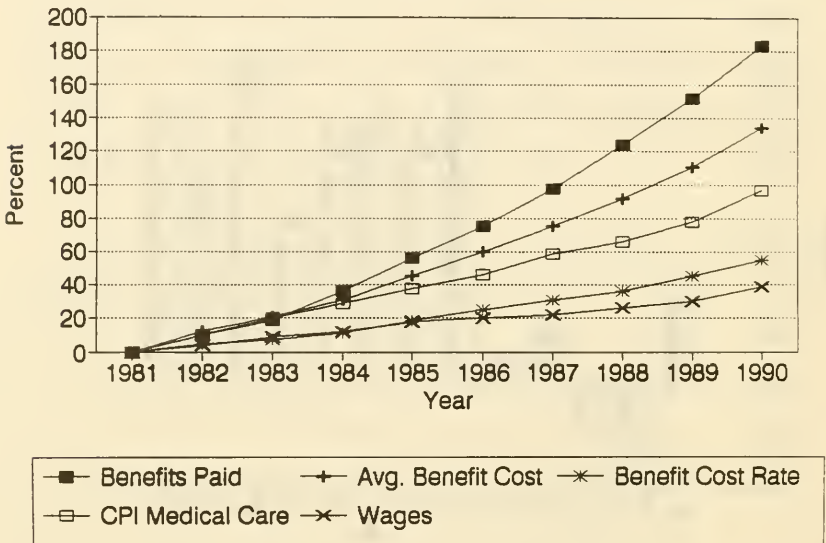
For the information of the Committee, I have attached a copy of a position statement signed by the Labor/Management Discussion Group on Workers' Compensation, a broad-based group comprised of labor, business, insurers and the medical community. The group is in agreement that the connection between medical and disability case management is an important one. Further, they believe that workers' comp can and should benefit from any cost containment measures enacted as a part of a new national health care system.

Thank you for allowing me to testify here today. NFIB looks forward to participating in the important debate over workers' comp and health care reform.

Average NCCI Premium Rate Changes



Workers' Compensation Benefit Costs 1981-1990



*Labor Management Discussion Group on Workers' Compensation***Workers' Compensation
and National Health Care Reform**

If a comprehensive national health system reform plan is adopted, then the following should apply:

1. The workers' compensation system should be able to share in any cost containment measures of a national health care plan.
2. Any plan should ensure the delivery of all reasonable and necessary care to injured workers. Where appropriate, treatment especially tailored to occupational problems should be available.
3. Any plan should recognize the important connection between medical case management and disability case management and the public policy goals of restoration of health and timely return to work.
4. The health care costs of occupational injuries and illnesses should be appropriately allocated to the industry and employer where the illnesses or injuries occur.
5. National health system reform should not alter the liability of employers for occupational injuries and illnesses, nor should it alter the exclusive remedy doctrine.
6. Any plan should recognize the need for the efficient collection of appropriate data concerning occupational injuries and illnesses, their causes, costs, and the means of preventing them.

June 25, 1993



3 9999 05982 959 6

Labor/Management Discussion Group on Workers' Compensation
Membership List

Labor

Dept. of Occupational Safety
and Health
AFL-CIO
815 16th Street, N.W.
Washington, DC 20006
(202) 637-5206

Building & Construction Trades Dept.
AFL-CIO
815 16th Street, N.W.
Washington, DC 20006
(202) 347-1461

Industrial Union Department
AFL-CIO
815 16th Street, N.W.
Washington, DC 20006
(202) 842-7842

Food & Allied Service Trades Dept.
AFL-CIO
815 16th Street, N.W.
Washington, DC 20006
(202) 737-7200

United Brotherhood of Carpenters
Health and Safety Fund of
North America
101 Constitutional Ave., NW
Washington, DC 20001
(202) 546-6205

Laborers Int'l Union of N. America
Safety and Health Committee
905 16th St. NW
Washington, DC 20006

United Auto Workers
Department of Safety and Health
8000 E. Jefferson Avenue
Detroit, MI 48214
(313) 926-5563

United Steelworkers
Safety and Health Department
Five Gateway Center
Pittsburgh, PA 15222

Business

National Assoc. of Manufacturers
1331 Pennsylvania Ave, N.W.
1500 North Lobby
Washington, DC 20004
(202) 637-3127

U.S. Chamber of Commerce
1615 H St., N.W.
Washington, DC 20062

National Federation of Independent
Business
600 Maryland Avenue, N.W., Suite 700
Washington, DC 20024
(202) 554-9000

Council of State Chambers of
Commerce
122 C Street, N.W., Suite 330
Washington, DC 20001
(202) 484-8103

National Council of Self-Insurers
Marriott Dr., Dept. 924.36
Washington, DC 20058

State Associations Group
National Assoc. of Manufacturers
1331 Pennsylvania Ave., N.W.
Suite 1500 North Lobby
Washington, DC 20004
(202) 637-3054

UBA
Union Center Plaza, Ste. 400
820 First St., NE
Washington, DC 20002
(202) 682-1515

Others

Alliance of American Insurers
1501 Woodfield Road, Suite 400W
Schaumburg, IL 60173-4980
(708) 330-8500

American Insurance Association
1130 Connecticut Ave., N.W.
Suite 1000
Washington, DC 20036
(202) 828-7100

Liberty Mutual Insurance Co.
175 Berkeley Street
Boston, MA 02117
(617) 357-9500

American Medical Association
Dept. of State Legislation
515 N. State
Chicago, IL 60610
(312) 464-4769

ISBN 0-16-044172-2



9 780160 441721